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Asia Pacific Energy Security and the International Status of China

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Outlook of Asia Pacific energy security

According to general views shared by international energy sector, energy security mainly consists of energy production safety, supply security and usage safety. In most cases, energy security refers to energy supply security, which is to get access to sufficient energy resources at reasonable prices at any time, in other words, first, escape the situation of neither supply insufficiency nor serious shortage; second, escape the situation of intolerable high oil & gas prices.

For the time being, the situation of international energy security is not optimistic: the main energy production fields unbalanced distribute in the Middle East and a few specific regions; maritime cargo, served as the main channel for hydrocarbon transportation, is suffering the pirate threat. Besides, in the long existing international energy system, the existing 50 giant "oil heritage projects" are controlled by Shell, Mobil, Exxon, Total and other 10 multinational European and American energy companies.

The global oil supply and demands have grown steadily in some decades, but this balance were broken due to the rapid economic growth of emerging countries in the Asian Pacific region, such as China, India, as well as Indonesia, Malaysia, Vietnam and other Asean countries, since the beginning of the new century. Almost all the above-mentioned countries have large population, the desire for better urban life of citizens stimulate the rapid growth of car manufactures, as well as many other heavy industries, which make oil and gas demand rise sharply.

Meanwhile, the overall Asian energy production scenery is not optimistic, no huge energy reserves have been found since 1970s (including in the Middle East). In coming years, demand is likely to continue bumping up against installed productive capacity. To describe the nowadays Asia-Pacific energy market, may we use one metaphor: *the supply is too old, the demand is too young?*

Although countries have been making great efforts to carry out new development and experiments, before alternative energy macro-levelly used, dependence on the energy supply of the Middle East will be getting higher and higher. According to the forecast of the UNEP, world energy dependence on Middle East oil will rise from 26% in 1997 to 40% in 2040. However, for each country, the dependence on the Middle East is different.

For decades, Japan and South Korea have established closed energy diplomacy with oil producing countries in the Middle East and Africa. China and India had no choice and just started to develop the relationship with the oil-producing countries, and try to get some of the upstream resources in order to protect energy supply security. However, as the world's major oil and gas producing areas has long been divided up by Europe and the United States energy companies, which make late-development countries, have made little progress. Therefore, in the future, Asia will be the key area as well as the vulnerable chain in the world energy market, once energy supply shortage encountered, Asian countries will suffer much than Europe and the United States.

Energy insecurity: how to mitigate the problems

Under the context of high oil& gas prices, energy insecurity have triggered series of troubles in Asia Pacific region. From one hand, acquiring as much as possible energy resources could cause the conflicts among different regional powers. For instance, disputes around the Chinese drilling platform called "Chunxiao" in the East China Sea between China and Japan, respective declaration of uninhabited islands in the South China Sea by China, Vietnam, Philippine, Malaysia, and Brunei, have absorbed international attentions from time to time.

From other hand, losing possession of essential energy resources could trigger severe economic and social problems, encourage the rise of nationalism, even lead to political turmoil. Under strong domestic pressure, no side would give in easily. Thus, the existing controversies could even deteriorate to the worst situation: maritime military conflicts.

To avoid the potential conflicts, there are some measures to be done.

1, setting up political and economic dialogue mechanism to resolve maritime disputes

After realizing the value of underwater resources, South China Sea surrounding

countries have struggled in succession to get possessions of isolated islands and nearby sea territory for almost 2 decades. Every claimant assumed respective historical arguments or international law, situations turned to be worse, players are more and more declining to use warships to control their maritime territory, and the chances for military clashes are increasing.

For many years Beijing insisted on using the policy of "detained dispute, explore together", derived from Five Principles for Peaceful Co-existence, to negotiate with its counterparts. Although result of persuade is not optimistic, it still provide a mechanism: political dialogue between governments and economic negotiations among different national energy companies might be better choices than confrontation and military competition in the controversial continental shelf. After all, the maritime dispute is rather closely related to economic resources than sovereignty in the continental borders, moreover, the exploring risk for maritime resources in this region remains very high.

2, increasing oil reserves to deal with emergencies

As for the "quantity security ", many developed countries have established their own strategic petroleum reserve. One of the preconditions becoming member state of the International Energy Agency (IEA) is that, one country must guarantee oil reserves within 90 days, such as the US Strategic Petroleum Reserve can maintain 120 days, Japan's reserves can maintain 169 days. Therefore, undoubtedly it is necessary to establish oil reserves to cope with threat for oil quantity security posed by emergencies in a short period of time. In addition, with the declining of international energy reserves and the growing of developing countries' demands for energy, in the foreseeable period of time energy prices will stay in the high level, the price of oil reserves can only continue to increase. The domestic sector can only choose the right time to procure in the international market at relatively reasonable prices, to meet the domestic demand for oil security and reduce the risk of oil price instability.

3, Constructing and strengthening the future energy market to acquire price-setting right

One of the functions of oil future market is to avoid crises. Under the condition of avoiding the future business, the grave market price crisis can only be shouldered by the government or enterprises. By avoiding the action of hedging, not only the nation oil reserve but also the enterprises oil reserve should bring down the fluctuation of oil market so that to ensure the price security of the oil industry. The right for oil price-setting is the display of a nation's international position and the comprehensive national strength. The current international oil price is defined by NYMEX and IPE's oil price market. As in Asia there is not a successful oil futures market so that the price that Middle East selling to the East Asia is over pricing than that of EU and US market.

Therefore, with the establishment of regional oil futures market rather than passively accept the international oil price, can Asian countries take advantage in defining regional oil price so that to get a favorable position in the international energy competition. Not long before, Singapore and Shanghai have successively build oil exchange and oil futures exchange bourse, they are of course, still lack of the supervision and experience comparing with the rest of the world.

Common energy market building: a response to the long-term supply threat

Today, important structural shift in the global energy market is the phenomenon of “Resource nationalism”, which means progressive concentration of the world’s oil reserves under the control of national governments and national energy companies, especially in the Middle East and the former Soviet Union. This phenomenon is also defined as national governments’ assertion of ownership rights over oil and gas reserves against the interests of international energy companies.

In Russia, the national energy company headed by Gazprom reinforced its position, although Russia has undergone leadership change in mid-2008, but Vladimir Putin's successor Alexander Medvedev determined to follow the route of Putin, so for Russia, the strategy of taking energy as a strategic weapon to regain great power status will not be changed. In recent years, Russia has been using energy diplomacy, Russia has energy conflicts with Ukraine, Georgia and Belarus and other neighboring countries, which raise the concern of EU.

Saudi Arabia using its unique status as the “swing producer” for the global oil market to cultivate a deepening strategic relationship with China and other new consumers as a “hedge” against precipitous deterioration in the Kingdom’s traditional strategic partnership with the United States.

With the spread of resource nationalism, many long term contracts have been terminated or faced the pressure of adjusting the cooperation conditions. Thus, the costs of the long-term energy supply to the Asia Pacific have been raised. In order to manage the volatility from the main, the consumers have to behave wisely. Take the case of Middle East, while dealing with such exporters like Iran, Iraq which are eager to develop their industries, can importers assign the pay-back contract, when deal with Saudi Arabia and Kuwait where the upstream is not open for foreign investors, PSA (private sector assessment) contracts are popular. Shortly speaking, more profitable the projects are, stricter the contracts will be.

Besides, as Middle East is the common supplier of Asian consumers, it’s strongly recommended to their companies to cope with suppliers in one voice, in order to alleviate the price premium which troubles most Asian countries for a long time.

A stable energy market is profitable both for suppliers and consumers; there is strong need for both sides to form a strategic alliance. Many technique measures

could be adopted to strengthen this cooperation; among them cross investment in the downstream area is very useful means which can ensure and deepen mutual interests for all the participants. Middle East is a very important area with complicated geopolitical situations, in order to secure the long-term energy supply, to deal with various producing countries differently, to construct interest community with all the game players, and to diversify energy supply in other regions as Russia, Central Asia and Africa are all choices for Asia Pacific consumers.

China's energy supply security

China became a net oil importer in 1993, before this year, China was an energy self-sufficient country. But with the rapid development of the national economy and the change of people's consumption patterns, China's domestic energy demand increased rapidly, while the energy structure is undergoing significant changes. At present, in China's current energy consumption structure, coal still accounts for about 70%.

As one of the world's largest Coal reservoir and producers, even in the middle of this century, the position of coal in the energy structure will not be replaced. Especially considering that the majority of rural residents in China have a low consumption, which makes China is bound to have long-term dependence on coal.

Due to the situation of China, China has stuck to the strategy of "coal -focused, electricity -based ". Because the existing oil and gas fields have limited production capacity, in order to realize the goal of "resource-saving and environment-friendly," from early 90's of the last century, China National Petroleum Corporation, Sinopec and CNOOC, have look into the international energy market, in addition, they increased oil and gas imports year by year, and entered overseas energy fields, began to control and develop the upstream resource. According to the plan, the proportion of oil and gas consumption will increase from less than 20% currently to 26% in 2010 and about 40% in 2020, of which the import of oil and gas will exceed the total consumption by 50 percent, the ratio of imports will bigger and bigger., China can not but consider increasing the proportion of high-quality oil and gas and other clean energy in the energy structure. At the same time, for urban residents, more housing, cheaper cars, more travel and more paid vacation, will be the lifestyle fashion, which makes China's oil demand increased significantly.

Therefore, oil supply security has gradually become China's diplomatic and strategic focus. China imported 120 million tons of crude oil and imports 40 million tons of refined oil in 2004, superior to Japan. Since this year, China become the second largest consumer after the United States in the world oil market.

At present, China's external dependence of oil consumption has surpassed 40%, the issue of national oil supply security has been highlighted. At the same time, fluctuation of the oil prices in international market has a profound impact on China's

economy, which makes oil security urgent. It is predicted that by 2020 China's demand will reach more than 400 million tons, while China's oil production is expected to reach only 160 million to 170 million tons or so, then there will be 240 million tons of oil gap.

From the perspective of the main source of China's crude oil imports, more than 80% of crude oil was imported from 10 countries in 2008, more than 60% from the Middle East and 5 countries of Africa. It is expected that over the next few years, the proportion of imported oil from the Middle East and Africa will continue to maintain a high level.

Seen from the current relationship among the major powers, the United States, Russia, Japan and other countries of China have contained China in the energy sector, the result of China's use of international resources is unsatisfactory.

As a result of the increasing reliance on the imported energy products, our government has adopted a series of measures to increase energy supply security, including:

1. Increasing domestic production. After multiple exploration of the sea and land-based fields, engineers have not found new oil and gas fields which are worthy of exploitation. The existing oil field, such as Daqing, Shengli, etc., has entered the post-mining phase; the quantity and quality are on the decline. While in western part of China the Tarim Basin, because of hidden depth and relatively high freight costs, which led to high development costs, it is difficult to substantially increase domestic production of energy products in the short term.

2. Increasing use of natural gas. In addition to large-scale use of coal and oil, the Chinese government has accelerated the construction of the project transport the natural gas from the West to the East and domestic gas distribution network in major cities and it also began the construction of large-scale liquid natural gas (LNG) loading and unloading dock in eastern coastal area. According to the International Energy Agency (IEA), the global natural gas in 1999 ratio of energy use is 23 percent, while China only accounted for 3%. China and Australia in 2002 signed import contracts of 12 billion US dollars for the liquid natural gas (LNG), not only because the situation in Australia is more stable than in the Middle East, but also in line with the principle of energy diversification and increasing use of natural gas.

3. Implementing plan of the strategic petroleum reserve. China in the international energy market has always been "buy low sell high", due to oil price each year; a large number of foreign exchange has lost. Before and after the Iraq war large swings in oil prices, resulted in worsening of domestic petrochemical enterprises and psychological panic of consumers, the reason lies in our country has no formal national energy reserve. At present, a small amount of oil inventories of petroleum

and petrochemical enterprises can only maintain for 10 days. In response to this grim reality, we have built four strategic oil reserves which based in Ningbo Zhenhai, Daishan in Zhejiang, Shandong Huangdao and Dalian, but because of high oil prices, at the end of 2007, Zhenhai has imported crude oil from Russian twice, the other bases have not yet been opened.

4. Implementing "going out" strategy. With Shell, Mobil, Exxon, Amoco and other transnational oil companies, it's not too long for China's energy companies to use offshore resources, so both experience and resources available are limited, at the same time, also facing many geopolitical and ideological obstacles, such as the CNPC(China National Petroleum Corp.) failed to acquire Russian Yugansk Oil Company and CNOOC(China National Offshore Oil Corp.) failed to acquire U.S. Unocal Oil Company, which can be a good interpretation of these difficulties. Nevertheless, China has made positive progress in opening up the international oil market since the mid-90s of the last century; Energy Companies, mainly including China National Petroleum Corporation, Sinopec and China National Offshore Oil Corp have established oil exploration and production partnership with 26 countries so far, and achieved the first step to the international cooperation and mining abroad. For example, China has purchased two wells in Venezuela and Kazakhstan, but Venezuela's oil production is at a late exploitation stage, while Kazakhstan's oil reserves, have not been clearly defined, so exploitation potential of the two wells are not great. In the near future, China imported oil still mainly from the Middle East.

5. Strongly advocating and promoting "conservation-minded society." The low overall price level of domestic public service goods, result in large and fast growth of China's energy consumption. However, since 2003, with the international oil prices rising, domestic related industries as well as the overall price level is also rising, and even prices of water, electricity and coal of public goods are also facing rising pressure. In this case, the Chinese government began to vigorously promote the construction of "saving society" so as to promote energy-saving building , using energy-saving products, encouraging people to buy micro-cars of small displacement , and formulated industry provisions for high-power appliances such as air-conditioning, and hoping that the efforts of the whole society can improve the energy efficiency, including oil so that less energy consumption can ensure the sustainable development of the national economy.

Geopolitical positions and China's state status

China's land is bordered on nearly 20 neighboring countries, including Russia, India, North Korea, while Japan and South Korea, with China's maritime power across the sea, from a purely geo-political situation, China's geo-space is very complicated, how to deal with relationship with so many neighbors is a natural test of China's diplomacy facing. China has long been facing the challenges of the land from ethnic and powerful neighbor in the northeast and northwest; And after the Opium War, it

has frequently been invaded by maritime power from the eastern and southern regions. Long land and sea borders, making China's national security severely tested, and limited military resources are always hard to cope with the dual challenges , therefore, in the late Ming Dynasty, China began to focus on the development of a continental country, in respect of the sea, are mainly national defense construction with shore-based defensive in nature . This geo-strategic choice existed until the beginning of this century. For the sea transport of energy, the Middle East and Africa are China's main oil import areas, the current hot spots of the international political and economic turmoil, where local conflict and terrorist incidents frequently occurred; and more than 90% of China's imported oil shipped from the sea, 90% of which is shouldered by the outer shipping. And transport fleet will be mainly through busy and narrow Strait of Hormuz and Malacca, there is no powerful Convoy Fleet, in event of war, diplomatic or other force majeure risks, China's oil transport security will be in a very passive situation.

But in the world, China has a very favorable geo-strategic advantage. The vast territory of our country lies not only in the center of Asia, but also in the geographical location of the best of the world: The eastern Pacific and is conducive to the outside world, especially opening up to developed countries such as Japan and the United States so as to acquire capital and technology, which is essential to promote economic development and trade expansion; The western region of Xinjiang directly borders Tajikistan of Central Asia, Kyrgyzstan and Kazakhstan and other oil countries , is also not far from such oil rich countries as Uzbekistan of the Caspian Sea and Turkmenistan , which provides the unique geographical access to oil resources for our country from Russia and Central Asian countries. The unique geo-economic advantages, is also quite special among the major powers in the contemporary world.

At present, China's relations with Asia Pacific neighboring countries are the best in the history. On north land borders, China and Russia have basically solved the border issue between the two countries for many years, through the establishment of the Shanghai Cooperation Organization and signing treaties, the two countries "strategic cooperation" is on a new legal basis. Economic and trade relations between the two countries are also developing rapidly. The establishment of the Shanghai Cooperation Organization will also help China to improve geo-strategic environment in Central Asia. In South Asia, China and Pakistan has always friendly neighbors, and after "9.11" the strategic partnership between the two countries has been further strengthened, China's relations with India have begun to return to a positive and healthy road. Although after the "9.11 ", the United States tend to expand in Central Asia, South Asia in military and political field, the strategic balance in South Asia have also been challenged, but China's stability in overall land-based strategic line has not fundamentally changed. In the Pacific, China has developed relations with North Korea as well as South Korea in Northeast Asia; the

relationship with Japan is also seeking cooperation in competition. Since the Cold War, economic and trade relations has continued despite Sino-Japanese friction, which has provided a solid foundation for a steady development of Sino-Japanese relations. In Southeast Asia, the comprehensive cooperative relations between China and ASEAN, has rapidly expanded in recent years .The "China - ASEAN Free Trade Area" plan has provided a broader stage for the further development of relations between the two sides .

With the deepening of economic globalization and continuously developing of the trend of international environment for reconciliation and economic development after post-Cold War, it's inevitable for China to become a regional great power, as a "responsible global power," the voice is also growing. Frankly speaking, economic globalization is the globalization of the commodity economy and consumer markets dominated by Western countries; China is one of the few developing countries which seize the opportunity to enjoy the benefits of globalization. However, the negative impact globalization has brought to China is obvious, as a "world factory", China's economic dependence and economic risks are both growing; At the same time, for the lack of profits ,a large number of foreign-funded enterprises acquire the core technology and intellectual property , the nation enterprises are in serious difficulties of development. The most serious problem is that a large number of high energy- consumed and low value-added industries are to China, causing serious environmental pollution and the domestic energy crisis. Therefore, the adjustment of industrial structure, the building of "environmentally friendly, resource-saving society" has become the choice of the Chinese government, the adoption of amendments to anti-trust case; also provide a legal basis for guiding and regulating foreign investment in China, and optimizing the industrial structure.

Strategy Options for Energy Safety

In order to solve the long-term security of energy supplies, China should start from the international relations and the specific energy supply channels, dealing with other major oil-producing countries such as the Middle East, and oil-consuming countries such as Europe and the United States leading the world's energy consumption pattern. Recently, China should continue to further develop cooperation with Saudi Arabia, Iran, Sudan, Nigeria and other exporting countries, in particular should pay attention to dealing with the United States and Russia.

Both China and the United States belong to the Asia-Pacific geopolitical pattern-oriented countries, geo-political competition is normal, but there is no basis for China and the United States to develop into the hostile opponent, the two countries have a wide range of common interests in maintaining regional stability, peace and prosperity; and strategic security areas such as the economic trade cooperation, environmental protection, non-traditional security areas. As for the area of energy, the United States and China are energy consuming and importing

country. These two countries have common interests in many of the world's energy issues, and have a good basis for cooperation. For example, both imported from the Middle East oil, both would like to jointly safeguard the security of oil transportation of the Middle East. As an independent force in international energy cooperation, the United States can not ignore China. Therefore, the two countries have common needs and foundation for cooperation in energy field, especially in oil and gas fields, they can have common ground while reserving differences so as to avoid the two countries become hostile opponents in the Asia-Pacific geopolitical competition and develop cooperation in energy, trade and other areas to promote peace and stability in the Asia-Pacific area.

China and Russia have long established strategic partnership of cooperation, political relations is the best ever. However, in contradiction with this is that the economic ties are not well-developed. Therefore, Russia and China should strengthen bilateral trade, increase mutual investment, and deepen mutual dependence; so as to lay a solid economic base for the development of relations between the two sides. Russian-Chinese oil cooperation is one of the best ways. To some extent, the China-Russian Far East oil pipeline project is not merely an economic contract problem, to some extent is an important benchmark to measure Russian-Chinese strategic partnership with a solid material foundation. For China ,it's key to have access to Central Asia's energy-exporting countries, such as Kazakhstan and Turkmenistan that she have always maintained good cooperative relations with Russia in energy area, additionally, it add weight to a wide range of energy imports channels .

With international oil prices rising, the prices of foreign oil with its unique rights and interests also increased, at the same time, taking China's economy as a whole into account, to some extent, it can offset the negative impact resulting from rising oil prices. Taking into account the high level international oil prices will remain for a long period, China should quicken the pace of overseas oil exploration. For this purpose, Beijing should formulate and implement a coordinated national energy strategy and foreign policy, use comprehensively political, economic, and diplomatic and other means, and implement a unified encouraging policy in terms of tax, foreign exchange, loans and credit guarantees.

China is undergoing tremendous transformations of continental nation to a ocean power, and such transformation would unavoidably draw attention of neighboring nations and international society. The topic of “China threat” has become the focus of the western countries for a long time. However, we should mention that China and western countries have different thinking and manage state affairs model. China's history is a development history which established on the divine land rather than the enlargement one. China has long attached great importance to its soft power, such as culture and economy's influence on its neighboring countries rather than

invading or occupying territories. China would revive and become the most influential country. Such revival does not mean sacrifice or damage other nations' interests and challenge the current international system as an ambitious rising power. It would pursue the principles of "peacefulness is prized" and "keep good neighborly and friendly relations" which filled with Chinese traditional humanism spirit and developmental pattern.

Conclusion

As the most important strategic commodity, oil& gas are closely related to the international politics. People should consider the global energy market as a whole when researching on the energy problem. One should not only understand the relationship between the regional element and energy issue. But also understand the energy security is the common goal under the tendency of globalization. It depends on how to deal with energy relations among the nations to a large degree. Sometimes such relations can displayed by competition, while on most occasions it must through dialogue, coordination and cooperation.

The energy security is the material foundation of China as a global power. To solve this problem; China is willing to be accepted by the global energy system. Beside Chinese government's own effort, all the producers and consumers should recognize that China's energy diplomacy is implementing by observing the regulations under the energy system. With the fast development of economy, China is increasing with geometric grading. Even the China's oil companies would not exploit overseas, it would satisfied its need by the international energy market. With the oil's scarcity, many overseas funds have considered the energy as the target of investment and speculation. In addition, the tangible and intangible elements all contribute to the high price of oil-centered energy commodities.

So it is unfair to criticize China as the culprit of the high oil price. Just as Daniel Yergin mentioned, it is a wise and imperative decision for China to incorporate international commerce and investment system rather than bargaining with other nations like a peddler. It is beneficial not only for China's energy security, but also for the global energy system. All the partners should have a clear reorganization of the integration. As the world have just one complex energy system, and its stability is very important for all the partners.

As for Chinese government, changing the developing paradigm and industrial pattern, guiding the reasonable consumption model so as to push sustainable development at home; effectively communicating with producers and consumers so as to get rid of security dilemma and eliminate the negative influence of "China threat". It's an important precondition of ensuring China's energy security and sustainable development.

For short run, the urgent task for Chinese government is to find solutions with Japan on East China Sea dispute, with Asean neighbors on South China Sea conflicts, without peaceful environments, no party can enjoy a sustainable development; for longer term, the main duty for all Asia- Pacific rim countries is to build up a common Asia Pacific energy market which is assumed to be a interest community. How to reach the final target? All the participants should devote politic wisdoms, economic compromise, and patience. And there is a long way for us to go.