

East Asia and the Middle East: A Fateful Energy Embrace

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Two thousand years ago China's Han dynasty traded extensively with Persia and Mesopotamia. For fifteen centuries a vigorous trade in silk, spices, and a variety of manufactures continued. In the past decade Beijing, Dhahran, Abadan, Mumbai, and Yokohama have grown ever more connected once again. The catalyst this time is energy. Across the vast swath of Asia south of Sakhalin, east of Xinjiang, and north of Sumatra—home to over a quarter of humanity—there is only one major oil field—Manchuria's Daqing. And that is rapidly declining toward depletion. Japan, Korea, and Taiwan have virtually no on-shore domestic oil or gas reserves at all. Whatever prospective hydro-carbons they have appear to be off-shore, and often in disputed waters of the East and South China Seas. The substantial oil and gas that China does appear to have are concentrated in the West and North, while the country's explosive growth centers along the southern and eastern coast. Even though China is the fifth largest oil producer in the world, its energy-infrastructure problems and rapid growth make it a large and growing importer, responsible for more than a third of the entire world's expansion in oil demand over the past four years.

Overall, the Asian region holds only around 3 percent of world oil reserves, and roughly 8 percent of global gas. It holds a substantial 23 percent of global coal, centering on China, which still satisfies 70 percent of that massive and rapidly growing nation's total energy demand from coal. Yet coal cannot, amidst an automotive revolution, supply China's rising demand for hydrocarbons, and is, in most forms, intensely polluting. Coal is no long-term solution.

The ultimate long-term solution to East Asia's energy insecurities lies inevitably in the Middle East. Saudi Arabia, Iran, and Iraq together hold nearly 43 percent of the world's proven oil reserves, and 21 percent of global natural gas. The Persian Gulf as a whole holds nearly two thirds of the world's oil, and around 40 percent of its gas. At current rates of consumption, the Gulf could supply the entire world for more than 26 years, or East Asia as a whole for nearly a century. Both East Asia and

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the Middle East, of course, have multiple potential partners in increasingly global and flexible energy markets. Russia is an especially important potential supplier, especially in natural gas. It holds over 30 percent of proven world gas reserves, with vast areas of tract-less Siberia remaining virtually unexplored.

Yet East Asia—much more than any other region in the world—is locked above all in a fateful energy embrace with the Middle East. In 2004 that volatile region supplied 70.8 percent of Asia's oil imports, as compared to only 23 percent of American overseas supplies. And the Middle East also provided 34.8 percent of Asia's gas. Asia's major nations vary marginally in their current energy dependence on the Middle East. Japan, for example, gets around 87 percent of its oil from the region, South Korea's dependence is 80 percent, and China's only 51 percent. Yet these are mere matters of degree. All face the long-run prospect of unavoidable Middle East reliance, given their rapid growth and lack of local energy supplies, combined with the formidable reserves that the Middle East, and especially the Persian Gulf, have at their disposal.

The inter-regional reliance that East Asia experiences with respect to the Middle East appears to be mutual: Asia is also the Middle East's largest energy customer, by far. In 2004 Asia took just short of two-thirds of Middle East oil exports: a full 64.5 percent. And it also took 52 percent of the Middle East's gas exports, with an ever-larger share in liquefied natural gas (LNG). Over the long-run, Asia's rising role in the global economy, combined with its energy insecurities, will make it an indispensable customer for much of the Middle East on economic grounds alone. And geopolitical considerations, including a desire by both regions for autonomy from the United States and Europe, could well deepen this cross-regional entente.

There is a parallel, if less urgent, logic for East Asian energy interdependence with Central Asia as well. Kazakhstan, with its massive Tengiz field, is rich in oil, while Turkmenistan and Uzbekistan, in particular, are rich in natural gas. Many have equated Central Asia's energy endowments with those of the North Sea. Central Asia has a particular attraction for India and China, due both to proximity and to the inescapable geopolitical reality that pipelines from Central Asia reduce their dependence on sea lanes from the Middle East currently dominated by the United States.

East Asian Strategies for Middle East Access

As befits a pattern of mutual interdependence that is both important and uncertain in its prospects, East Asia's approach to Middle Eastern energy questions is a multi-faceted one, that emphasizes neutralizing the

inherent risks. The approaches of all the key Asian nations—Japan, China, South Korea, and India—have parallel trade, investment, and national-security dimensions. All four countries—most interestingly China—are also actively striving to diversify their energy relationships away from the Middle East—even at economic cost—so as not to be caught up too deeply in its regional political complexities.

On the trade front, Asian nations have been active in soliciting long-term contracts, and in providing goods and services to the Middle East so as to defray the cost of rising energy imports. Japan, Korea, and China have all been active in Middle East construction, ever since the first Oil Shock of the 1970s. With the run-up in energy prices over the past two years, they have geared up their export strategies once again. China, for example, recently garnered contracts for the first two stages of the new Tehran metro system, and stands a good chance of landing the rest of the related construction business as well. Korean construction contracts in the Middle East surged 65 percent in the first half of 2005, to \$6.2 billion.

The dynamic area now is that of long-term investment in energy development and distribution, which could transform the Asia-Middle East relationship, “from a courtship into a marriage”, in the view of many observers. During October 2004, for example, China’s Sinopec Group concluded a gas agreement to import more than 270 million tons of natural gas over the next 30 years from Iran’s South Pars field in the Persian Gulf, the largest natural-gas reserve on earth, which Iran shares with its small neighbor Qatar. This project will bring Iran \$70 billion in hard currency over the coming three decades. The deal also gives Sinopec a half-share in one of Iran’s most important new discoveries, the Yadavaran field in southwest Iran, allowing Sinopec to explore for oil there over the next few decades. With the field’s oil reserves estimated at around 17 billion barrels, China’s operations there could be worth another \$100 billion, in return for substantial investment.

Japan has also made recent commitments to invest heavily in the Middle East. After Japan’s Arabian Oil Company in February, 2000 lost the Kafuji concession in Saudi Arabia that it had held since 1957, the Japanese government concluded a deal to develop the huge Azadegan oil field in Iran, only ten kilometers from the Iraqi border, in February, 2004. Japan’s total investment is to be \$2 billion, over a contract period of 12 and a half years, stretching to late 2016. The prospects for the deal are clouded by the Iranian nuclear problem and U.S. opposition, but Japan clearly faces strong competitive pressures from China if it does not go ahead with the Azadegan project—pressures that are painfully intensified by the short contract period.

India is undertaking two major new energy projects in the Middle East, also focusing on Iran. The first is a \$4 billion gas pipeline, stretching 2775

kilometers from Iran's massive South Pars natural gas field on the Persian Gulf to the west coast of India, via Pakistan. The second is an ambitious \$22 billion long-term project providing for Iran to supply India with 5 million tons of LNG annually, for 25 years from 2009.

With Middle East relationships taking on increased geostrategic importance for Asia, as the economic scale of those relationships increases, and as energy prices rise, Asian nations are taking a variety of steps in the national-security realm to safeguard their interests. It is by no means accidental that South Korea and Japan had, in the fall of 2005, two of the largest contingents of peace-keeping forces still remaining in Iraq, apart from the United States and Britain, or that Japan was one of the largest Official Development Assistance (ODA) donors to the Palestinian authority, as well as five of the seven Central Asian states, most of them major energy producers. China's deepening presence in Iran, as well as its reported stationing of 4,000 non-uniformed forces in the Sudan, both seem to be closely related to its oil interests.

Neutralizing Future Energy Insecurities

Clearly Asia will want to hedge its future bets on the volatile global energy future. While deepening ties with strategic Middle Eastern energy producers such as Saudi Arabia, Iran, and potentially Iraq, Asia will simultaneously want to diversify its conventional oil and gas supplies away from that turbulent region, to the extent that it realistically can. China, in anticipation, has been consorting with African oil producers such as Angola and Congo, while all three major Northeast Asian countries—Japan, China, and South Korea—have been courting Russia as well.

Given its energy efficiency and environmental friendliness, Russian gas is a rational alternative to oil, and especially to Middle Eastern oil, for Asia. With nearly a third of global reserves—and possibly more in the unexplored recesses of Siberia—Russia is a natural supplier, and especially to Asia. When the North Korean nuclear crisis is resolved, a more developed regional gas pipeline network could become a serious prospect, paralleling the emergence of extensive regional gas networks in Europe and North America in earlier years. Nuclear power will also be an inevitable element of Asia's hedge against Middle East volatility. Japan and South Korea are already among the most substantial producers of nuclear power on earth, together with France and Sweden. And China is projected to be the largest generator of nuclear power on earth by 2050.

Yet in the end, the inexorable arithmetic of global energy supply and demand will continually force the Middle East and Asia back into interdependence with one another. Hydro-carbon supply, to put it

simply, is in the Middle East. And demand, fueled by remarkably relentless economic growth, is in Asia. Indians consume about one barrel of oil per person, China two, and the U.S. twenty-eight barrels per person annually. As developing Asia modernizes, the supply to meet its aspirations for a mobile, affluent life-style will have to be in the Middle East, that region's ceaseless troubles notwithstanding.