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## Fueling the Superpowers: Potential Hazard for U.S.-China Relations

Travis Tanner  
*Chinese Studies, the Nixon Center*

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## Fueling the Superpowers

## Potential Hazard for U.S.-China Relations

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*This article by Travis Tanner is taken from the proceedings of the EPIIC Symposium at Tufts University, February 2005*

**I**n February 2005 crude oil futures prices jumped to exceed \$51 a barrel. In conjunction with terrorist risk premiums, China's surging demand for oil is a major driver behind the soaring prices. In fact, since the beginning of 2000, China has accounted for 40 percent of the growth in world oil demand.

Oil is an essential ingredient in China's successful formula for economic growth, especially owing to the fact that China is at an oil-intensive stage of development. It is critical for driving industrial activity, generating power, constructing infrastructure projects, and fueling the rapidly growing number of automobiles on Chinese roads. Today there are 25 million vehicles on the road and that number is projected to double by 2010 and reach 150 million by 2020. China's domestic oil production is flat, and therefore, in order to meet its growing appetite, China has been a net oil importer since 1993. Today, imports comprise 35 to 40 percent of China's total oil consumption, growing 31 percent in 2003, and by 2020 some estimates put China's dependency on foreign oil as high as 70 percent. As the rapidly growing economy further expands and the populace becomes wealthier, demand for oil will continue to swell.

Oil consumption in the United States, the world's largest consumer of petroleum, is expected to grow nearly 50 percent over the coming twenty years. Beijing, also on the fast-track to oil dependency, is currently on a search to secure energy sources across the globe. This quest, in addition to China's heavy reliance on Middle Eastern oil (roughly one-half of its imports come from there), suggests a potential rivalry between the United States and China over access to oil-rich regions. Many analysts argue that the trajectories of the world's two most voracious oil consumers will inevitably lead to a clash over the scarce resource.

*Travis Tanner is Deputy Director and Assistant Director of Chinese Studies, the Nixon Center, and author of The Oil that Troubles U.S.-China Waters.*

Will the United States and China actually square off in a war for resources sometime during the first half of the century? The potential for a coming collision over the world's limited oil reserves does, in fact, exist. But several essential considerations must be examined before drawing such a conclusion.

First, until recently, China's energy strategy has appeared disjointed, often fixed on multiple mutually exclusive objectives and quite often designed to meet political ends at the expense of economic considerations. As a result of instability in the Middle East and the need to maintain economic growth as a means to achieve social stability, however, Chinese authorities have recently approached the nation's energy policy in a fundamentally new way. Foremost, in contrast to the long-standing strategy of advocating self-reliance supplemented by oil imports from the Middle East, Beijing has embarked on a diversification strategy both in terms of the development of alternative fuels and the establishment of new oil-import markets. In the PRC's State Council November 2003 report, it was officially declared that China plans to pursue an energy development strategy focused on securing "a diverse energy mix."

Examples of Beijing's desire to reduce its dependence on foreign oil and to expand its energy mix include the following: the recent move to solicit bids on four newly proposed nuclear power reactors, increased oil imports from its current importers, such as, South Africa, Iran, Oman, Sudan, Angola, Vietnam, Yemen, Indonesia, Russia, Kuwait, with special focus on boosting imports from Central Asia, Russia, and Africa. Additional examples include: the ongoing construction of three large liquid natural gas projects along the Chinese coast, plans to establish a strategic petroleum reserve, plans to increase offshore exploration, and continued interest in the construction of a number of pipelines (Kazak; Russia; Turkmenistan). CNPC has acquired oil concessions from Kazakhstan, Venezuela, Sudan, Iraq, Iran, Peru, and Azerbaijan.

One example that clearly illustrates Beijing's relatively recent shift toward and focus on energy security policy is the recent decision to move forward on construction of the Kazakhstan-China oil pipeline. In 1997, at the time the original agreement was made, the 3,000-kilometer pipeline from Kazakhstan to China made little commercial sense when compared to the alternative of having oil imported from international markets and delivered to China's eastern coast via tanker. The deal instead was part of Beijing's strategic efforts to partner with Central Asian nations to protect against potential proindependent uprisings along the Xinjiang border as well as to counter growing U.S. presence in the region. In fact, after seven years, only the first 400 kilometers of the pipeline had been completed. The recent push to finish up the second, much larger, section of the project demonstrates Beijing's latest yearning to lock in new energy supplies and diversify away from Middle Eastern oil.

Second, technological advances in the oil industry and the development of alternative energy sources will allow, over time, energy users to become more efficient and decrease their overall reliance on oil. As China's economy expands further, competitive enterprises will develop and adopt new technology, which will result in more efficient energy use. Presently, China is well behind the United States in energy efficiency. In 2001 China's energy users spent \$151 billion, approximately 13 percent of GDP as compared to the United States where energy use comprised only 7 percent of GDP.

No one knows when Earth's remaining oil deposits will dry up, but almost all experts agree that before mid-century the world's oil supply will "peak" — marking a change from an increasing supply of cheap oil to a dwindling supply of expensive oil. Therefore, the technological advances required shifting away from oil reliance toward substitutes such as natural gas, hydropower, biomass, and other renewables are not only welcome but necessary. In the future, when the cost of developing and utilizing alternative energy sources equalizes with the cost of oil use, simple economics will drive rapid progress in these areas. Oil dependency will decline as it becomes more economical to take advantage of alternative energy sources. In fact, the United States Department of Energy forecasts a decline in oil prices from current prices well over \$40 a barrel today to \$27 in 2025 as a result of new exploration and production technologies as well as alternative sources of energy.

The third factor to be contemplated when analyzing the likelihood of a future U.S.-Sino oil clash is the dynamic bilateral relationship these two powers share. Since dialogue began in the early 1970s, progress on strategic, political, cultural, and commercial levels has flourished and resulted in a very strong, mutually beneficial relationship. As a sidebar, it is interesting to note that Colin Powell remarked on several occasions that U.S.-China relations are the best they've been in thirty years; while in China recently, I had several officials and scholars comment that the current state of U.S.-China relations has reached a level of maturity not previously obtained. During the Bush administration, two strategic points of convergence have arisen: North Korea and terrorism. For example, in the realm of commercial ties, the United States has become China's second largest trading partner while China has become the United States' third largest trading partner. The large number of shared interests not only provides incentives for avoiding a showdown over a single limited resource, but also provides multiple spheres in which cooperation and diplomatic arrangements can be worked out. In fact, last summer the two nations agreed to launch the U.S.-China Energy Policy Dialogue, which will expand energy related interactions and cooperation between the world's two largest energy consumers.

So the question remains: Will growing demand for oil sour the U.S.-China relationship to such a degree that a collision is inevitable? I contend that

China's newly evolving energy strategy, technological progress in the oil industry and the increasingly robust bilateral relationship make this claim unlikely.

I do believe the potential for this rivalry certainly exists and that energy concerns could prove to have a significant negative impact on the relationship. I'd like to enumerate a couple of points that illustrate this:

- 1) In its current pursuit to secure energy resources, China has adopted a mercantilist or almost zero-sum approach. Beijing perceives the United States as encircling and pursuing a containment strategy against it. It is worried about sea lane security — for example, were a crisis to break out in the Taiwan Strait, it fears the United States would cut off vital sea lanes — such as the Straits of Malacca — which would cause major oil supply disruptions. Furthermore, China is concerned by the large and likely long-term United States presence in the Middle East — to a degree, it buys into the argument that the United States was driven by oil concerns to invade Iraq; China sees itself operating outside the large multinational oil corporations based in the United States and is afraid of the implications of this. Moreover, Beijing views the relatively new and robust American military bases in Central Asia and long-standing U.S.-Japan alliance as potential threats and part of an effort to contain China. There are mixed messages in the Chinese response to the Angarsk to Nakhodka pipeline on the one hand and the Kazak-China pipeline on the other. This perception of being threatened and encircled by the United States is aggravated by energy concerns and has detrimental effects on the state of the bilateral relationship and if continuously fueled, over a considerable amount of time, could develop into a serious hazard for bilateral ties.
- 2) Another geopolitical consideration is China's increasing involvement with nations the United States deems unfriendly like Sudan and Iran. The Chinese signaled strong opposition toward the proposal in the UN Security Council in 2004 to implement sanctions on Sudan. In light of the fact that China and Iran recently signed a \$75-100 billion oil and gas deal, what would be the implications for U.S.-Sino relations if the United States were to propose taking similar actions toward Iran? This is a hot spot that has the potential to flare up and cause major damage to the relationship.
- 3) Certain Americans have found China's recent efforts to secure energy resources in Canada and Venezuela (the United States depends on both for one-quarter of its oil imports) as a Chinese attempt to sneak into the United States by a back door and deemed this behavior as potentially threatening to U.S. national interests. Additionally, CNOOC has considered purchasing Unocal — an American oil company — a move that could add fodder to the "China threat" fire in the United States. The proposition really makes sense because the company mainly does business in Asia but this could stir up a backlash on Capitol Hill.

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**What Can the U.S. Do?**

- 1) First and foremost, it's not in the United States' interest to have an energy-starved China.
- 2) The United States can help China slow down its demand growth — should cooperate on new technology and promote efficiency. U.S.-China Energy Policy Dialogue is a step in the right direction. The forum's aim will be to increase collaboration in high energy and nuclear physics, fossil energy, energy efficiency and renewable energy, and energy information exchanges (pollution-free hydrogen; nuclear fusion; natural gas; oil recovery technology).
- 3) Move forward and encourage regional cooperation in Asia to reduce angst over supply disruption. The United States should promote the formation of an entity like an Asian IEA.
- 4) The United States should also take steps to further strengthen the existing bilateral relationship across the board including the realms of economics/commercial; diplomacy; cultural; security. Should take whatever additional measures needed to dispel the notion that the U.S. is encircling China.

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**What Can China Do?**

- 1) Tax fuel consumption more effectively.
- 2) Leapfrog to cleaner cars.
- 3) Tighten up restrictions on vehicle efficiency.
- 4) Migrate to gas as soon as possible.

Maintaining a robust economic growth is seen as a top priority by the leadership in Beijing. Economic growth is key to job creation, job creation is key to maintaining social stability, and, of course, social stability is key to ensuring the CCP's authority and legitimacy.