

CHINA IN CENTRAL ASIA: ENERGY INTERESTS AND ENERGY POLICY

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Introduction

In the mid-1990s, China displayed the first flickers of interest in the Central Asian fuel and energy complex, which has been steady-

ly growing since that time along with Beijing's interest in other spheres of the region's economy. In the latter half of the last decade of the 20th

century, the project activities of China and Chinese companies in the Central Asian energy segment were concentrated in Kazakhstan's oil and gas sector. In the early 21st century, however, this interest began gradually spreading to the rest of the region to become diversified by the industry's branches. Today, China is showing a lot of

interest in the oil and gas of Kazakhstan and Turkmenistan and in the nuclear power production of the former. China is paying enough attention to the fuel and energy complexes of the rest of the region to promote its economic and political interests in each of the states and the region as a whole.

The Role and Place of Energy in China's Strategies

Domestic policy. China's general strategy is geared toward boosting the efficiency of the planned and centralized state administration and management of its ramified and dynamically developing economy, while liberalizing economic activities at home. This calls for a balance between the traditional socialist and the capitalist conceptual and ideological attitudes, principles, and goals designed to preserve the country's integrity and security and ensure its sustainable development. The national-state ideology and the leading role of the Communist Party of China are never questioned.

This means that the Chinese fuel and energy complex is intended to ensure consistent development of all the economic segments, social and economic stability, and stronger military and political might. China's energy policy was and is concentrated on the following:

- (1) stage-by-stage development of the domestic raw material base of the national fuel and energy complex;
- (2) its accelerated technological modernization; and
- (3) diversification of national power production by using all types of energy sources.

Foreign policy. China is seeking a place among the key players on the global economic and political scene. It is placing its stakes on greater efficiency and attractiveness of the Chinese economic model while trying to find a niche for the country in the global processes and the quest for mechanisms of their efficient management badly needed to preserve its integrity, sustainable development, and security, as well as its position in the world.

Applied to the energy sphere, the above means that Beijing should protect its economic interests and its influence in the global and regional energy markets by acquiring firm positions in long-term contacts with fuel-rich countries (the Central Asian countries included) to guarantee a consistent inflow of raw materials into its fuel and energy complex. Today, its interests are concentrated on hydrocarbons; tomorrow they will spread to uranium. This is not an end in itself, but rather the country's readiness to cooperate with other countries, particularly its neighbors, in order to guarantee China's strategic interests in the economic, security, and political spheres.

The role and place of Central Asia. On the whole, Central Asia plays a secondary role in China's security and raw material (energy resources) spheres: it is a strategic rear to be relied upon for greater political efficiency (in the security, economic, and energy spheres) of China's relations with the leading Western countries and APR neighbors, which are priority vectors for China.

In other words, China's strategy based on carefully studied and analyzed international experience (Soviet experience included) is being successfully realized as part of a long-term devel-

opment program/algorithm. The Chinese intend to build a strong and self-sufficient state able to survive global and regional calamities and prevent security threats in every, including the energy, sphere.

The fact that this strategy underestimates the fundamental importance of the Eurasian heartland and the potential of strategic partnership with the Russian Federation and Central Asia can be described as one of the main faults of China's strategic course. This, however, is largely predetermined by Russia's and Central Asia's policy in the energy sphere, which is still limited to the interests of national companies and geared toward larger fuel exports.

This explains why China regards Russia and the Central Asian countries as unreliable and temporary allies rather than strategic partners; in the energy sphere, their role is limited to fuel and raw material supplies. The interests of Russia and the Central Asian countries (including in the energy sphere) are threatened by the factors described above rather than by Chinese policy per se. Energy- and raw-material-related rivalry between China and Russia and the Central Asian countries cannot be totally excluded.

The Central Asian Fuel and Energy Branches in China's Economic Policy

In the post-Soviet era, China's economic policy in Central Asia has been consistently placing greater importance on the region as one of Beijing's domestic and foreign policy energy-related priorities.

In the first half of the 1990s, China's economic interest in Central Asia was fairly limited, concentrating mainly on Kazakhstan and Kyrgyzstan. In fact, at that time, the Central Asian countries never considered China an important economic partner, their hopes being pinned on Russia and the West, as well as on some of the financially attractive and culturally close Islamic states.

By the middle and end of the 1990s, China clarified its interests in Central Asia to help promote the newly launched program of accelerated development of its inland territories. This interest developed into the first projects of Chinese companies in the oil and gas sector of Kazakhstan and the much more prominent presence of Chinese producers in the region's consumer markets. By that time, the Central Asian countries had already developed an interest in China as an important economic partner; they needed larger volumes of imported Chinese consumer goods and machine-building products.

Early in the 21st century, Central Asia's importance as one of China's foreign economic factors was boosted by the changed economic, energy, and geopolitical factors. In the wake of 9/11, the region, which had so far remained in the backwater of world development, found itself in the center of hectic political activities. Beijing augmented its economic presence in Central Asia: it intensified its project and investment involvement, even though this was still limited to the region's mineral and fuel riches. Chinese producers expanded their presence in the Central Asian markets; larger loans started flowing into the Central Asian economies. This meant that Beijing identified the economy as a linchpin of its Central Asian strategy.

The Central Asian countries, in turn, learned to look at China not as an important trading partner, but as a strategic investor/creditor for their economies.

China's rapidly growing economic presence in the region and its bilateral and multilateral economic relations (including in the fuel and energy complex) with the local states are still far from the

ideal and from historically justified cooperation patterns; they hardly fit China's long-term interests or those of the Central Asian countries and Russia.

On the one hand, China's economic presence is limited to producing and importing industrial raw materials (fuel in particular), which depletes Central Asia's resources, does nothing for its processing branches, and steps up competition or even rivalry with the Russian Federation. On the other hand, the fact they have no or a weak industrial policy and strategy of economic integration into the post-Soviet expanse is forcing the Central Asian republics (wittingly or unwittingly) to perpetuate their status of "raw material (energy resources in particular) appendages;" they are gradually degenerating into targets of the current global resource and influence game.

This does not fit the logic of positive development trends in the Eurasian heartland; the most unfavorable scenarios—a clash of Chinese and Central Asia or Chinese and Russian interests—look possible; they are doing nothing for the sustainable economic development or security of Russia, Central Asia, China, and other countries of continental Eurasia.

China's Economic Policy and Energy Interests in Each of the Central Asian Countries

China and its companies are mainly interested in the oil and gas sector of Kazakhstan and Turkmenistan,¹ the hydrocarbon and export potential of which look preferable. So far, the oil and gas sector remains the core of China's economic and energy regional policies; the Chinese, however, are showing much more interest than before in other economic branches as well.

In recent years, China has been demonstrating a lot of interest in nuclear energy (Kazakhstan); power production (Kazakhstan, Tajikistan, Uzbekistan, and Kyrgyzstan); and coal mining (Kyrgyzstan). This means that China is gradually spreading its economic influence to Tajikistan and Kyrgyzstan, two countries with no considerable hydrocarbon resources, and Uzbekistan with considerable (so far not exported on a great scale) oil and gas reserves.²

¹ The proven oil reserves of **Kazakhstan** are assessed at about 5.4 billion tons (about 3% of the world's total); the figures for gas are about 1.8 trillion cu m (about 2% of the world's total). The proven oil reserves of **Turkmenistan** are assessed at about 100 million tons (about 0.06% of the world's total), and gas reserves at about 2.9 trillion cu m (3.2% of the world total) (for oil reserves, see: June 2006—L.S. Beliaev, V.V. Bushuev, M.R. Lastovskaia, A.V. Lebedev, O.V. Marchenko, P.A. Sergeev, S.V. Solomin, S.V. Filippov, *Mirovaia energetika: sostoianie, problemy, perspektivy*, ed. by V.V. Bushuev, Enerzia Publishing House, Moscow, 2007, p. 588; gas related information can be found in *Oil&Gas Journal*, No. 103.47, 2005, pp. 24-25—L.S. Beliaev, V.V. Bushuev, M.R. Lastovskaia, A.V. Lebedev, O.V. Marchenko, P.A. Sergeev, S.V. Solomin, S.V. Filippov, op. cit., p. 587). The official oil and gas figures for Turkmenistan are slightly higher than those quoted by respectable foreign sources. Turkmenistan assesses its oil reserves at 15 billion tons, and gas at about 24 trillion cu m (see: *Gazovaia industriia Turkmenistana: perspektivy razviva*, Information portal TurkmenInform (Turkmenistan), 24 April, 2009, available at [<http://www.turkmeninform.com/ru/press/2009/04/25/0000981.htm>]).

² Uzbekistan is one of the world's leaders with respect to gas production; its forecasted reserves are about 2.2% of the world's total. Its share in the world's total gas production is 2.5%. In 2008, its proven gas reserves were assessed at over 2 trillion cu m; oil reserves at 82 million tons, and gas condensate at 160 million tons. The figures for the republic's forecasted gas reserves are 5.9 trillion cu m; for oil, 817 million tons of oil; and for gas condensate, 360 million tons. In recent years Uzbekistan has been producing over 60 billion cu m of gas, between 40 and 49 billion cu m of which are used inside the country; 10 to 16 billion are exported. At the same time, Uzbekistan depends on oil imports, this dependence increasing even more in the future. In 2010, it will have to buy no less than 4.2 million tons of oil (see: the site of the National Information Agency of the Republic of Uzbekistan [<http://www.uza.uz>]; the site of the National Holding Uzbeftegaz [<http://www.uzneftgaz.uz>]).

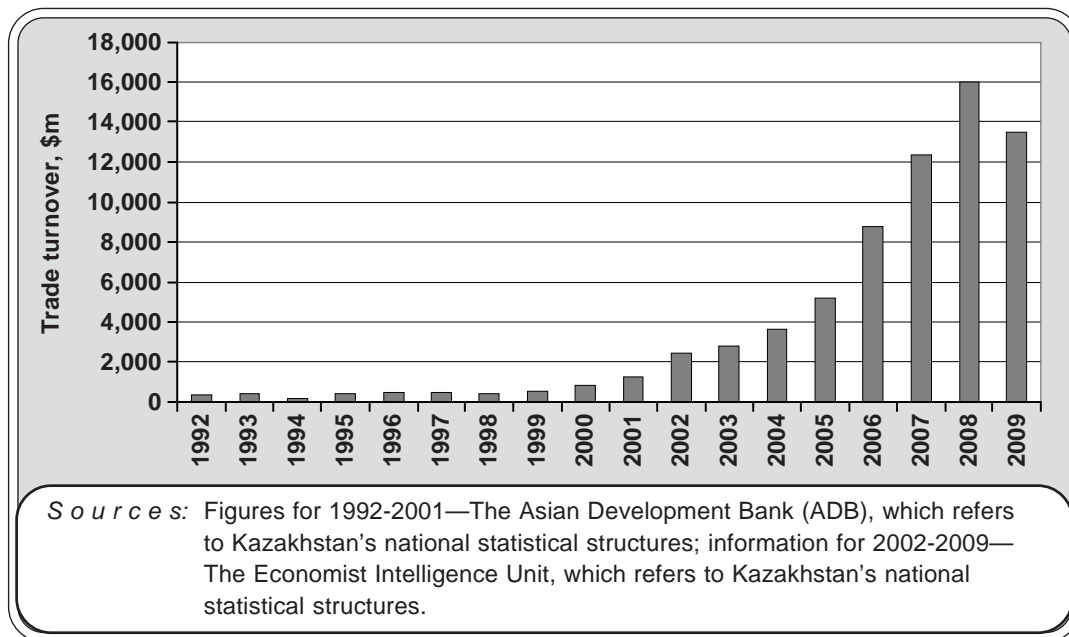
Kazakhstan

From the very first days of their diplomatic relations, China has regarded Kazakhstan as the key target of its economic and energy interests in Central Asia. In the first half of the 1990s, however, its economic presence in Kazakhstan was limited mainly to trade. In the latter half of the same decade, however, China demonstrated much more interest in the energy sphere, mainly because Chinese economy developed into a major energy consumer (oil in particular). Chinese companies came to Kazakhstan with their projects and their money; the leading energy corporations of China became interested in the assets of Kazakhstan’s oil and gas branch and involved in the development of hydrocarbon fields in the country’s west.

In the first decade of the 21st century, China’s presence in Kazakhstan’s economy and its energy sector became even more pronounced. China’s widening presence in the republic’s market is best illustrated by the following figures: between 2001 and 2008, China increased its deliveries of commodities 11.3-fold: from \$0.74 to about \$8.4 billion; the total trade turnover increased from \$1.25 to about \$16 billion. In 2009, the volume of Chinese exports to Kazakhstan dropped by 10.5% against the previous year and accounted for \$1.514 billion; while the total trade turnover dropped by 15.5%, to \$13.482 billion (see Fig. 1).

Figure 1

**Trade between China and Kazakhstan
(1992-2009)**



The trade structure, however, testifies that Kazakhstan was obviously a raw material source; in 2008, for example, over 93% of its exports to China were raw materials (*energy fuels accounted for about 82% of the total*; ferrous and non-ferrous metals for about 12%). Kazakhstan bought products of the machine-building and metal-working industries (about 53%), foodstuffs and consumer goods (about 35%), and other commodities from China (see Table 1).

Table 1

Structure of Trade between China and Kazakhstan (2008)

Description of Goods	Supplies from China to Kazakhstan		Supplies from Kazakhstan to China	
	\$m	Share, %	\$m	Share, %
Chemical products	—	—	266	3.5
Ferrous and non-ferrous metals	—	—	1,156	15.2
Energy resources	—	—	5 549	73.0
Machinery and equipment	3,412	40.8	—	—
Foodstuffs and other consumer goods	2,968	35.5	—	—
Other	1,004	11.7	631	8.3
Total	8,362	100	7,602	100

Sources: The Economist Intelligence Unit, which refers to Kazakhstan's national statistical structures (*Kazakhstan: Country Report*, The Economist Intelligence Unit, London, March 2010).

After identifying Kazakhstan as the main target of its trade, economic, and energy interests in Central Asia, China launched a much more active lending policy, favorable loans going mainly to the projects developed by Chinese companies. Oil and gas were not the only targets of Chinese investments: loans went to other economic branches as well.

On the whole, China's total investments in Kazakhstan's economy amount to no less than \$23.6 billion, including about \$11 billion in investments, \$0.55 billion in loans, and \$12.1 billion in assets³ bought in various (mainly oil and gas) industries; the fuel and energy complex received over 93% of the above.

On the whole, China's economic (and energy) presence in Kazakhstan can be described as considerable; China and Chinese companies are still involved in the raw material sector despite Astana's frantic efforts to channel Chinese interests into the processing branches and industrial and innovation cooperation.

Kyrgyzstan

From the very first days of their diplomatic relations, China has regarded Kyrgyzstan not as a market to be filled with Chinese products, but mainly as a strategic foothold from which Beijing could expand its trade in Central Asia and the post-Soviet expanse. The trade relations between the two countries intensified after 2004.

³ Figures for the beginning of 2010.

Figure 2

**China's Trade with Kyrgyzstan
(1992-2009)**

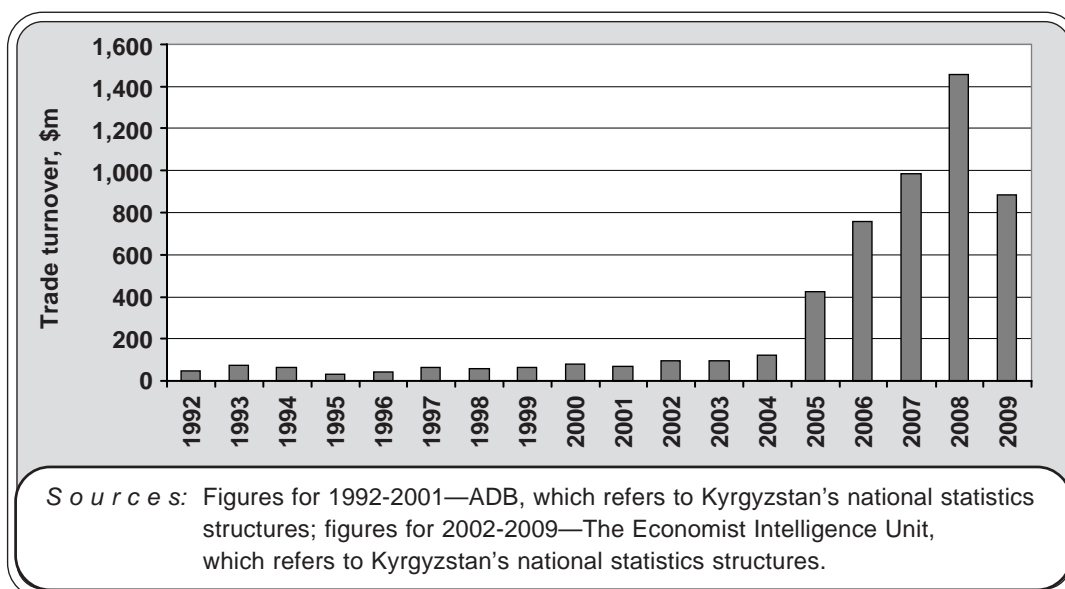


Table 2

Structure of Trade between China and Kyrgyzstan (2008)

Description of Goods	Supplies from China to Kyrgyzstan		Supplies from Kyrgyzstan to China	
	\$m	Share, %	\$m	Share, %
Chemical products	168	14.2	—	—
Ferrous and non-ferrous scrap	—	—	155	58.0
Machinery and equipment	60	5.1	—	—
Textile raw materials (hides and wool)	—	—	74	27.7
Consumer goods and foodstuffs	735	61.9	—	—
Other	223	18.8	38	14.3
Total	1,186	100	267	100

Sources: The Economist Intelligence Unit refers to Kyrgyzstan's national statistics structures (*Kyrgyzstan: Country Report*, The Economist Intelligence Unit, London, March 2010).

In 1992-2004, the volume of Chinese commodities in the Kyrgyz market remained within an annual limit of \$26-100 million, while trade turnover was at the \$30-125 million level. In 2008, the volume of Chinese exports reached \$1,186 million with a total turnover of \$1,453 million. In 2009, the volume of Chinese trade with Kyrgyzstan dropped from \$1,186 to \$528 million; total turnover decreased from \$1,453 to \$657 million (see Fig. 2).

The structure of Chinese-Kyrgyz trade shows that Kyrgyzstan is and will remain a source of raw materials. In 2008, Kyrgyzstan exported mainly ferrous and non-ferrous scrap (about 61%) and textile raw materials (mainly hides and wool, about 30%) to China. China supplied Kyrgyzstan with foodstuffs and consumer goods (about 72%); chemical products (about 10%); and machinery and equipment (about 4%) (see Table 2).

So far, China's presence is limited to trade; Chinese investments in the Kyrgyz economy are estimated at between \$160 and \$189 million (about 5% of the total is invested in the fuel and energy sector), \$120 million of which were issued as loans and \$40-60 million as investments.⁴ China's financial presence is mostly felt in small-scale mining, transportation projects, the production of construction materials, and technical aid to the republic's government. Projects in the fuel and energy complex, therefore, are few and small even for Central Asia.

Tajikistan

Until the middle of the first decade of the 21st century, China's economic presence in Tajikistan was limited to sporadic supplies of small batches of "Made in China" consumer goods. This is easily explained by the civil war of 1992-1996, the fragile peace which took many years to be consolidated, and the fact that Tajikistan is geographically isolated from China.

Their common border (over 500 km long), which passes through a high mountainous region and until recently lacked transportation infrastructure, isolated the two countries from each other rather than encouraged trade contacts. Chinese commodities reached Tajikistan via Kazakhstan, Kyrgyzstan, and Uzbekistan.

Tajikistan was the last of the Central Asian states to sign a border agreement with China, which proved to be the first step toward more active contacts through the Karasu checkpoint and the highway across the Kulma Pass; China issued favorable loans, mainly to purchase Chinese consumer goods.

Trade gradually began gaining momentum; in 2005, it grew more than nine-fold against the previous year to reach \$229 million. In 2007, the trade volume almost doubled; and in 2008, it grew by another 10%. In 2009, trade turnover dropped by 17.3% against the previous year—from \$755 to \$624 million (see Fig. 3).

Intensified trade between the two countries led to more active involvement of China and its companies in all spheres of the Tajik economy; between 2005 and 2009, Chinese business acquired a fairly strong position in the republic's key economic sectors, the energy sector in particular.

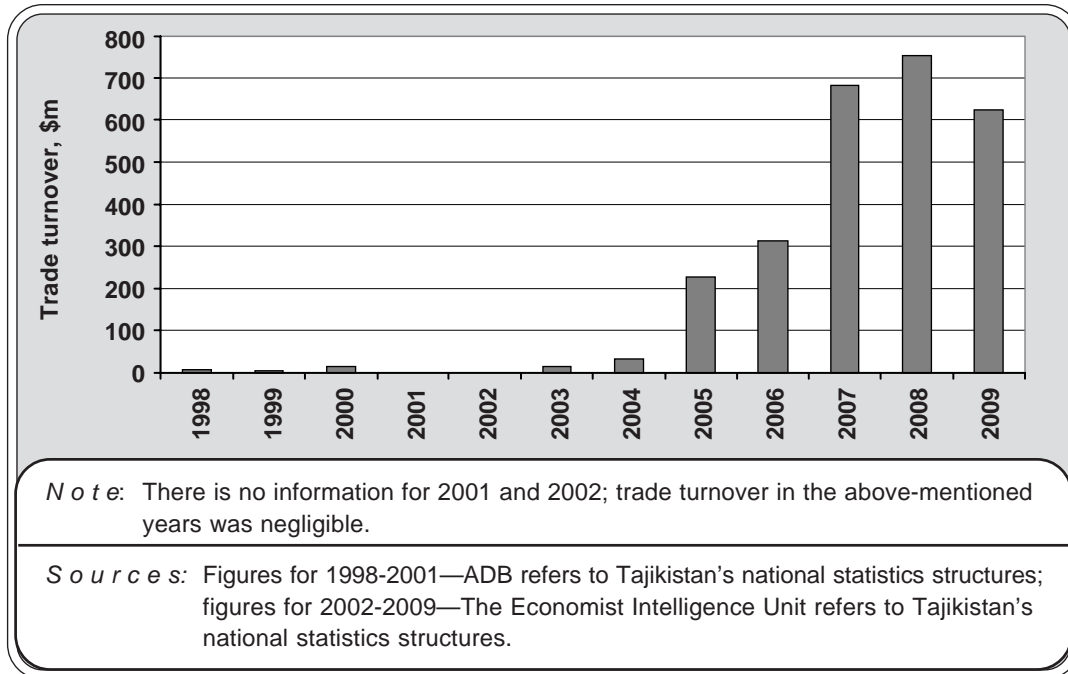
China's tested practice of easy loans on all sorts of economic and social projects made it the main creditor; it left international financial organizations and other countries far behind. The loans, as a rule, are used by Chinese companies. On the whole, China's financial resources in the republic are assessed at \$732 million (the fuel and energy sector accounts for about 44%), including \$600 million in loans, \$50 million in investments, and \$82 million in bought assets.⁵

⁴ Figures for the beginning of 2010.

⁵ Figures for the beginning of 2010.

Figure 3

**Trade between China and Tajikistan
(1998-2009)**



Turkmenistan

Until the middle of the first decade of the 21st century, China showed no intention of expanding its economic presence in Turkmenistan, which is explained, among other things, by the countries' geographic location. For a long time, the share of Chinese producers in the Turkmenian market was practically indistinguishable even on the small scale of Turkmenistan's foreign trade.

After 2006, however, as soon as Beijing clearly identified its long-term strategic interests in the republic's gas sector, China's economic presence in Turkmenistan became much more noticeable. In 2006, trade turnover more than doubled to reach \$125 million. In 2007, it grew another three-fold to reach \$377 million. In 2008, trade turnover increased by 76% (\$663 million); deliveries from China reached the \$568 million level. In 2009, trade turnover increased by 58% against the previous year to reach \$1,048 million (the share of Chinese exports being \$915 million) (see Fig. 3).

The recently shaped trade structure indicates that China exports machinery and equipment to Turkmenistan to be used by the Chinese companies working in the Turkmenian oil and gas sector.

In 2008, for example, 90% of China's exports were products of the machine-building and metal-processing industries; Turkmenistan sold energy resources (about 81%), cotton and other textile raw materials (about 6%) to China (see Table 3).

Project and investment activities of the Chinese companies involved in Turkmenistan's oil and gas sphere, as well as in the branches of special interest to Ashgabad, continued along with the rising trade volumes. There too, China relied on the mechanism of soft loans tested in other Central Asian countries.

Figure 4

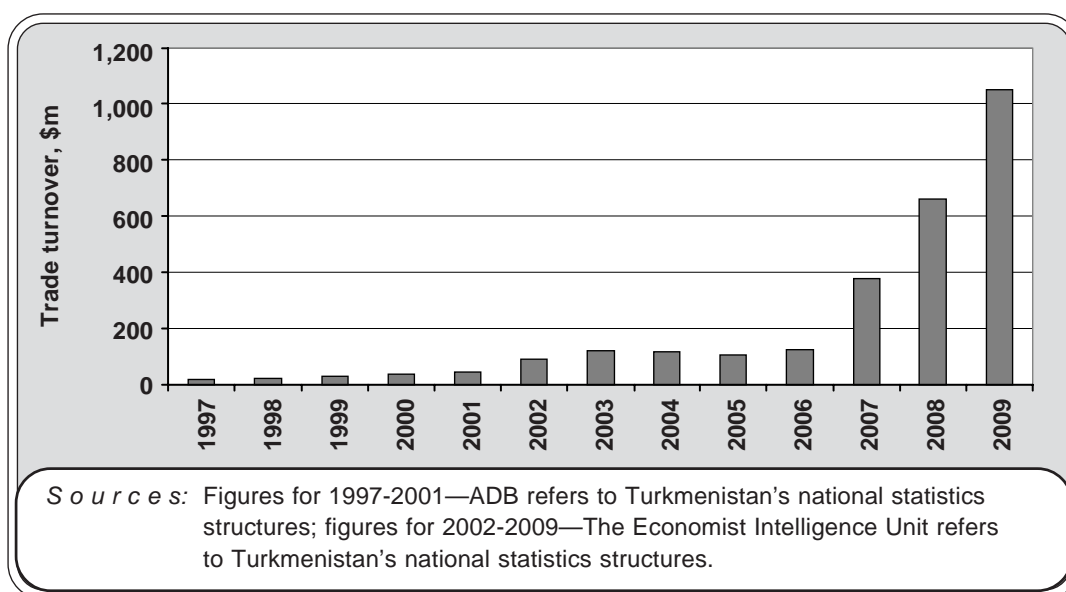
Trade between China and Turkmenistan
(1997-2009)

Table 3

Commodity Pattern of Trade between China and Turkmenistan (2008)

Description of Goods	Supplies from China to Turkmenistan		Supplies from Turkmenistan to China	
	\$m	Share, %	\$m	Share, %
Textile raw materials	—	—	7	6.8
Energy fuel	—	—	80	84.5
Machinery and equipment	524	92.2	—	—
Foodstuffs and consumer goods	28	5.0	—	—
Other	16	2.8	8	8.7
Total	568	100	95	100

Sources: The Economist Intelligence Unit refers to Turkmenistan's national statistics structures (*Turkmenistan: Country Report*, The Economist Intelligence Unit, London, March 2010).

The total volume of Chinese financial resources in the Turkmenian economy is estimated at over \$1.1 billion (42% in oil and gas), including about \$700 million in loans and \$450 million in invest-

ments.⁶ As a rule, the money thus extended and equipment supplied from China are used by Chinese companies involved in projects being implemented in Turkmenistan. The republic, in turn, responds by giving China fairly wide access to its oil and gas industry.

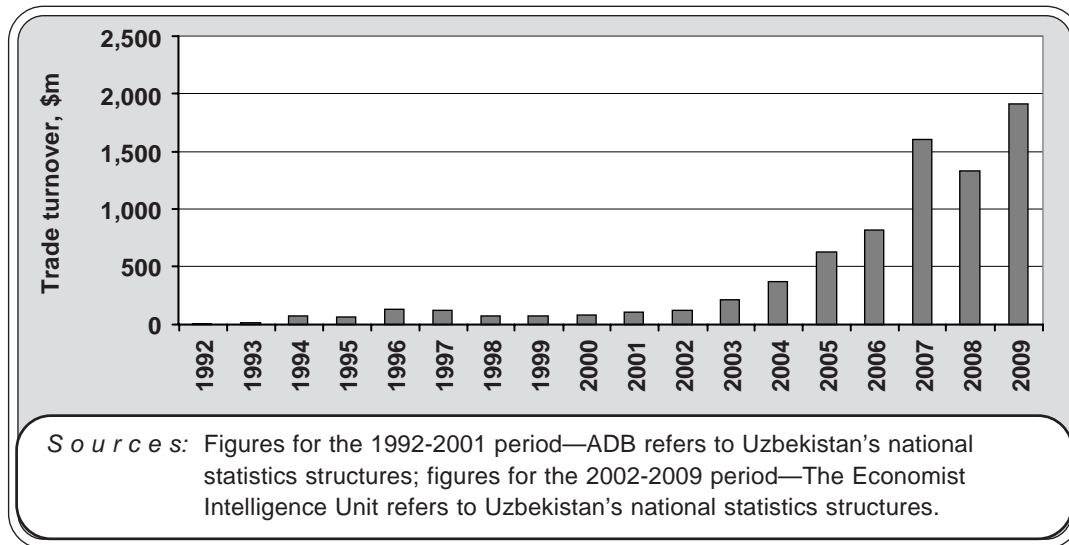
Uzbekistan

Throughout the 1990s and early 21st century, China could not, for several reasons, consolidate its economic presence in Uzbekistan. Until the end of 2002, economic ties between the two countries were limited to trade; after 2003, China began augmenting its economic involvement in Uzbekistan.

Between 1992 and 2002, China’s exports to Uzbekistan never exceeded the \$114 million level every year, annual trade turnover being \$136 million. In 2008, China exported \$791 million-worth of goods to Uzbekistan, the annual trade turnover being \$1,335 million. In 2009, trade turnover between the two countries increased by 43% against the previous year to reach \$1,910 million. The volume of Chinese exports grew 1.83-fold and reached \$1,453 million (see Fig. 5).

Figure 5

**Trade between China and Uzbekistan
(1992-2009)**



On the whole, Uzbekistan exports a much lower volume of raw materials than its Central Asian neighbors; however the structure of its trade with China reveals a fairly big share (40%) of raw material exports. In 2008, Uzbekistan exported cotton (about 15%); non-ferrous metals (about 11%); raw chemical materials (about 10%); and machinery and equipment (about 9%) to China. China sold Uzbekistan machine-building products (about 59%); foodstuffs (about 8%); and chemical products (about 11%) (see Table 4).

⁶ Figures for the beginning of 2010.

Table 4

Commodity Pattern of Trade between China and Uzbekistan (2008)

Description of Goods	Supplies from China to Uzbekistan		Supplies from Uzbekistan to China	
	\$m	Share, %	\$m	Share, %
Cotton	—	—	86	15.8
Chemical products	90	11.4	55	10.2
Non-ferrous metals	—	—	61	11.3
Ferrous metals	85	10.7	—	—
Energy fuels	—	—	23	4.2
Machinery and equipment	465	58.8	51	9.3
Foodstuffs and consumer goods	62	7.9	—	—
Other	89	11.2	268	49.2
Total	791	100	544	100

Sources: The Economist Intelligence Unit refers to Uzbekistan's national statistics structures (*Uzbekistan: Country Report*, The Economist Intelligence Unit, London, March 2010).

China relied on tied credits to be used to buy Chinese goods and services to consolidate its greater presence in Uzbekistan's trade turnover. Chinese companies intensified their involvement in the republic's project and investment sphere.

They are interested in several economic sectors, particularly the fuel and energy sector and related industries (oil and gas, energy production, and the chemical industry). The total volume of Chinese financial resources in Uzbekistan is assessed at no less than \$640 million (up to 85% of which is invested in the fuel and energy branches), including \$167 million in loans and \$473 million in investments.⁷

Conclusion

China, which depends on energy resources for its sustainable economic development, is very concerned about its energy and economic security. Its energy strategy consists of three major vectors:

- Attracting foreign investments and high technologies to modernize the national fuel and energy complex and related industrial branches (power engineering industry); the main hopes are placed on the West rather than on Russia or the Central Asian countries;

⁷ Figures for the beginning of 2010.

- Guaranteeing the uninterrupted supply of energy resources and electric power from abroad; Central Asia and Russia are seen as important, yet hardly priority, partners;
- Expanding China's internal energy base by increasing the production of energy resources on its own territory⁸ and energy generation.

It seems that there are several reasons for China's interest in Central Asian energy resources.

- *First*, the region is attractive both geographically and strategically: one of China's closest neighbors, it is part of the Eurasian heartland, which means that China (with no strong navy to be used to defend its interests in the World Ocean) can rely on the energy routes from Central Asia as being fairly secure because of its common land borders and stable bilateral relations with the countries of this region. Beijing spares no efforts to maintain political and diplomatic relations at this level.
- *Second*, Kazakhstan, Turkmenistan, and Uzbekistan boast fairly large deposits of oil and natural gas, the production of which can be increased; this means that these countries can be regarded as alternative and additional sources of hydrocarbons.
- *Third*, Kazakhstan and Uzbekistan are rich in uranium (used for nuclear power production), which adds another dimension to China's greater interest in the region: Beijing's plans in this sphere are very ambitious indeed.
- *Fourth*, Central Asia is very attractive as a possible transit area for Iranian and Mid-Eastern energy resources: the land routes, much shorter and much cheaper than the currently used U.S.-controlled marine routes, are potentially much more profitable and effective; the fact that the region has a ramified system of pipelines (some of them going toward Iran) adds to its attraction.
- *Fifth*, theoretically, the hydropower potential of Kyrgyzstan and Tajikistan is fairly tempting, however in the short-term perspective the large-scale development of these two countries' hydro resources is unlikely to become an important factor for the simple reason that water and energy are the region's sore spots. Uzbekistan and, to a lesser extent, Turkmenistan and Kazakhstan (which heavily rely on the region's water resources) are very concerned about the intention of Kyrgyzstan and Tajikistan (which control over 90% of the region's water resources) to build fairly large hydropower stations in their territories.

It does not seem likely that the water and energy problem will be resolved in this economically and politically fragmented region. China prefers to keep away from this very sensitive issue: hydropower projects are fairly expensive and slow on their returns. Beijing has opted for the wait-and-see policy because, irrespective of its involvement in the Central Asian hydropower projects, the Xinjiang Uighur Autonomous Region of China is the closest and commercially most attractive market. So far, the Central Asian countries and Russia as their partner are being left to sort out the region's water and energy problems themselves.

⁸ There is information that recently China has been following in the U.S.'s footsteps to gradually limit domestic production of non-renewable energy sources and increase exports. It is still too early to describe this as a stable trend.