

C H I N A

C O N V E R S A T I O N S

I N T E R V I E W

FAREED MOHAMED I & MICHAEL KLARE

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I N T R O D U C T I O N

ENERGY NOTES: MICHAEL KLARE and FAREED MOHAMEDI.

There is currently no greater sphere of competition than that between China and the United States in the field of energy politics. Oil and gas sectors (as well as other resource sectors such as steel and iron) are seeing fierce competition between the two powers, both seeking to ensure control over the goods that help keep their economies booming. It is through resource politics that the US is hoping to contain its 'peer competitor' and through which China hopes to ensure its economic dominance this century. The energy tussle is one of the more vital backdrops to the *'New Cold War'*.

For anyone interested in China and the US and energy politics, Michael Klare, author of *Blood and Oil: The Dangers and Consequences of America's Growing Dependency on Imported Petroleum* (Metropolitan Books 2004), is a good place to start. His first book, published after 2001, *Resource Wars – the New Landscape of Global Conflict* (Metropolitan Books 2001) first raised the issues of the Caspian Sea, the importance of Afghanistan, as well as many other regions seeing the intersection of geo-politics and energy.

His commentary has opened a necessary window on the energy tussle between US and China that is determining the redrawing of geo-political arrangements and boundaries in Eurasia and Asia. The war in Afghanistan, the war in Iraq and the overt energy diplomacy of Central Asia attest to the nexus of oil and gas and geo-politics. To quote English geo-politician Halford John Mackinder:

'Who rules East Europe commands the Heartland; Who rules the heartland commands the World Island; Who rules the World Island commands the World.'

The heartland in this quote refers to Eurasia, which includes Central Asia. The economic/energy rivalry in Central Asia between China, Russia and Western interests is being labelled *'The New Great Game'*. The comparison is made with the struggle between the British and Russian empires for control over Central Asia a century ago, a struggle in which Mackinder took part.¹

The oil deposits of Iraq are a factor in the current US occupation of that country. The invasion has successfully allowed Western interests to control the oil out of the country, thus limiting China's energy supply, a key factor in Chinese growth. Jonathon Storey, (one of the top energy experts regularly quoted in Washington) has written extensively about the intersection of geo-politics and China's energy needs, just one paper being *'The Global Implications of China's Thirst For Energy'*. This paper is fascinating for the way it links energy, geo-politics, and maritime strategy – something that questioned officials on either side rarely do 'on record' despite the obvious connection.

'Michael Klare tells us why the National Energy Policy of the Bush administration announced in 2001, is so important. It stated that the pursuit of 'foreign energy' was a major foreign policy objective - and that the US administration should 'engage in international diplomacy for this purpose.'

Of course China has its own national objectives – economic growth being paramount – and thus is scouring the globe, attempting to shore up investments in resource rich nations. As a result, both powers are jostling for influence in Africa, Latin America, Asia and Eurasia. This has led to the Chinese guarding pipelines in Africa and Cold War politics being played out in these small nations as both powers attempt to increase economic and political visibility.

The one incident that has so far highlighted the link between energy and national security concerns in America is the attempted takeover of UNOCAL, an American oil company by SINOOC, a Chinese firm. This was blocked on national security grounds in the House of Representatives and inserted into the energy policy of 2005.

The idea of energy policy as a sophisticated lever for a China containment policy is a common enough argument in Washington. The articles of John Mearsheimer from the University of Chicago, reveal the simple logic that China's economic and military growth is predicated on the access to energy supplies of the thirsty 'peer competitor'.²

Within Asia, maritime boundaries are linked to the resources under them – oil and gas – as much as the geo-political issue of 'naval capabilities', which allows Western interests to ensure that *'the Dragon'* has little opportunity to access the oil and gas, thus slowing its economic growth. Of course, as Michael Klare notes this can be applied to many areas around the globe.

I first heard Fareed Mohamedi from PFC Energy speak at a conference at Columbia University, the Second Annual China Symposium: *Feeding the Giant: The Domestic and*

Global Impact of China's Energy Needs.

'.. the policy of Wolfowitz and Cheney going back to the first Bush administration, and in fact the strategic reviews they did back then reflected this sort of thinking – and that is, in 1991 or 1992 they said 'we are at a historical crossroads. The Soviet Union has collapsed, we are the sole superpower, and we can remain the sole superpower for ever and a day. And who is the only threat on the horizon? And that's China.'

He states that the reason for the Iraq invasion was to diminish the power of Iraq and its oil – and to telegraph the ability of the US to control oil output in the Middle East:

'We took control of Iraq make another Saudi Arabia and diminish the power of that superpower and its oil. Unfortunately for them, we really screwed it up, but you can say that the control of oil is telegraphed to China. And China – even if the primary objective is not to control the oil to control China - the Chinese think it is.'

Mohamedli also rejects the line put forward by Washington that China is being 'mercantilist', not playing by 'fair' rules.

'The Western International Oil Companies have used their governments as much as the Asian National Oil Companies....I don't think that what the Chinese are doing is any different than what the Americans did, what the British did, what the French did with Total and South Paz....'

He also touches on the strategic importance of the maritime waterway known as the Straits of Malacca (adjoining tsunami-ravaged Aceh in Indonesia). Mohamedli describes it as an area where the US can threaten energy supplies to China, or where China can use marines 'to unblock its supplies....or use submarines to secure its defense around its own periphery.'

The importance of this point is apparent to all those that have followed the debate over which powers should be allowed to monitor the Straits, an issue that has seen the US call for Indian and Australian naval monitoring, those two allies firmly in the US sphere of influence. Obviously, the US is keen to see Western interests patrol the Strait – and keep China out.

In sum, these two interviews will tell you much about how vital energy politics is being played out between the two competing powers.

1 Igor Torbakov 2/04/04 'Reexamining Old Concepts About The Caucasus and Central Asia' A EurasiaNet Essay

2 Mearsheimer's articles are required reading for anyone wanting to argue that American foreign policy has been about 'engagement' with China. An article in Foreign Policy 2005 where he sparred with Zbigniew Brzezinski in an article called 'Clash of the Titans' is just one example.

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*Blood and Oil: The Dangers and Consequences
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OWL BOOKS, 2005.

Keady: You say that China's energy demands are fuelling a geo-political contest. Is China's growing demand for energy feeding into geo-politics?

MK: Of course you have to begin with history, as China is really new to this, and partly its newness is a matter of so much concern and discussion. It's not that it is doing anything any different from any industrialized power, but it has suddenly come from nowhere to become a major consumer of oil. It overtook Japan in 2003 to be the second largest consumer of oil and, years ago, nobody would have predicted that. Again, it is partly the novelty of a 'third world' country suddenly becoming a major consumer, so I put that in the background.

But secondly, more importantly, most of the existing world's known reserves are already claimed - claimed by the oil companies that have been in the business for over 100 years in some cases, for a very long time, and already have long term established reserve assets in many parts of the world. Then you have the national oil companies, Saudi Aramco and the others, so most of the world's oil reserves are already spoken for.

Along comes China, which seeks to join the company of oil consumers and oil owners, and finds a world in which most of the properties are already taken, from their perspective. So they're in a hard position. They either have to outdo, outbid Western companies for available assets, and that raises the hackles of some people. For example, when China bid 200 billion dollars more than Chevron for ownership of the UNOCAL corporation in June 2005, that was deeply concerning to American oil people because they raised the price, they forced Chevron to increase its bid. It makes the competition more intense.

On the other hand, China has forged ties with countries that have largely been neglected by the West for political reasons - namely Iran, Sudan, and to

some degree, Uzbekistan. These are in the American parlance, rogue states or pariah states and American companies are not allowed to do business there because of their anti-American political position. So along comes China and it's cutting deals with these countries, and this is considered a political, even a military challenge for the United States because in some cases China has provided arms and military aid to the countries it is doing oil deals with, like Sudan and Iran. So it enters into the geo-political interests of the United States, partly because having been excluded historically from ownership of oil, it sees no choice but to do deals with pariah states.

Keady: Well, oil is a military resource, isn't it? Is the oil quest linked to 'well, this might feed into their military might'? Is that part of the equation?

MK: It's part of the equation in the sense that most of China's imported oil now travels by ship from the Persian Gulf, like Japan's and South Korea's and Taiwan's – travels by tanker from the Persian Gulf countries, including Saudi Arabia and Yemen, Oman – through the Strait of Hormuz, the Indian Ocean, the Straits of Malacca, to China. And the Chinese are very worried that in a war with the United States, or over a crisis in Taiwan, the US could always cut off the flow of oil by sea to these sea lanes. These are areas where the US is the dominant force and it could do that with ease, and the Chinese would have no resist. So the Chinese are very worried about the vulnerability of their oil supply and so they are engaged in a strategy of diversifying their energy supplies, and this has led them to establish ties with countries they would prefer they weren't, like Venezuela for example, and Algeria.

China is competing in areas where it has been dominated by the United States, because those areas such as Venezuela would diversify their supply line. But also in particular China is trying to establish a landline to Central Asia, to Kazakhstan, it's now building a pipeline from Kazakhstan to China which would be vulnerable to cut off of supplies from the US Navy presumably, and this has made China seek a geo-political influence in Central Asia. Now this is an area where the United States also competes for geo-political influence and wants to play a very dominant role because of its interests in the Caspian Sea. So you have a geo-political competition between the US and China in Asian countries, with Russia also playing a role in all of this, and this has gotten ugly with the call by the Shanghai Co-operation Organization in July 2005 calling for the US to pull back its military bases in Central Asia. So here again, China's search for energy security is causing friction with the United States.

Keady: How significant is the oil and gas from, say, Iran and Russia? How significant are those?

MK: None of them is huge – they all represent a fraction of China’s imports. But because, as I say, China is very nervous about being overly dependent on one or two suppliers, so it is pursuing a strategy of diversification of multiple suppliers, and wants to have access to as many different suppliers as it can. It would like to have more oil and gas from Russia because, again, that could come from internal supply lines. The Chinese would love to build pipelines from Siberia to China. So far the Russians have been a little bit coy about this, for geo-political reasons. Iran is a potential supplier of natural gas, because it has the second largest supplies of natural gas in the world. So the Chinese are avidly seeking access to Iranian gas as well as Iranian oil. But really they are looking everywhere.

Keady: As I understand it, a National Energy Policy was announced by President George Bush – where he announced a diplomatic quest of sorts on energy he couched it in diplomatic terms. Is that correct and is it true China has a similar diplomatic framework for its energy quest?

MK: Yes, you are exactly right. Both of them are behaving in a similar way, with the chief executives of the US and China taking personal responsibility for the pursuit of overseas energy supplies. Now in the United States this is enshrined in a National Energy Policy of May 17 2001, which calls for the President of the United States to make the pursuit of foreign energy a major foreign policy objective, and calls on the Secretary of State and Commerce and Energy to engage in international diplomacy for this purpose.

Now in particular, what they are calling for is diplomatic pressure on foreign suppliers that have largely state owned oil industries, to open them up to American corporate or foreign investment, and also in places where the existing legal and taxation structure is an impediment, and calls on the President and his top people to negotiate, to clear the playing field, to open up the gates for American investment. For example, in the Caucasus where Kazakhstan has an inherited legal system that makes it hard for American companies to invest and take profits and so on. So it calls for the President and the Secretary of State and so on, to negotiate with those governments to smooth the involvement of American companies in their industry. Likewise in Africa, they call on the Presidents and Secretaries of State to negotiate with Nigeria, Angola, to make their legal system more amenable to foreign investment. Same with Mexico and

Venezuela, where the US would like to be able to invest and, in accordance with these injunctions, the President has engaged in personal diplomacy. He has met several times with Vladimir Putin trying to persuade Russia to facilitate, to ease investment in companies in the Russian energy industry. Likewise, the Secretary of State, Colin Powell made trips to Africa to open up African countries to American companies. So this is a policy that has gotten a lot of attention on the US side.

And in a very similar manner, President Hu Jintao of China has made pursuit of energy a personal matter, and he has traveled around the world seeking to open up countries to Chinese investment. His first trip abroad was to Kazakhstan interestingly enough, and the purpose of his first trip was to sign agreements on the shipment of Kazakh oil to China, and this pipeline that is now under construction. He's also met repeatedly with Vladimir Putin, for the purpose to persuade Putin to free up more Russian oil and gas to China. He has traveled to Brazil. He has met President Chavez of Venezuela in Beijing and talked about energy co-operation, and he traveled to Canada, his own backyard, and spoke openly about China acquiring access to Canadian tar sands. So he too, like President Bush, has made it a personal quest.

Keady: Well, I understand in Sudan, they have troops guarding a pipeline. Correct?

MK: It is my understanding that the Chinese have assisted Sudan in military operations against the rebel forces of the SPLA, certainly in providing support for Sudanese helicopters and planes, and providing training, and perhaps more than that as well. The United States provides troops for pipeline protection in Columbia and in the Republic of Georgia.

Keady: John Mearsheimer from the University of Chicago talked, a couple of years ago, about the containment of China, and possibly doing this via economic means. If you limit China's oil supply, isn't that effectively what you are doing?

Do you think this is part of an economic containment?

MK: I have certainly come across statements from hardliners in the United States that the US should try to block in China's quest for foreign energy –and this is from people with a very strong anti-China bias. This is not the policy of the Bush administration – and it is not official US policy. Official US policy is to encourage China to be a good capitalist member of the international market,

and to be free to purchase energy like any other member of the international community.

What the US objects to is China acquiring ownership of foreign reserves, direct ownership of oil and gas, and monopolizing its flow to China. But the US hasn't objected to China simply having access to the international market. My sense is that American leaders, that are Republican leaders at this stage in time, are ambivalent about the rise of China. They understand the American economy has been closely integrated with the Chinese economy, that it is very advantageous for many American corporations if they thrive, if they buy American goods, and so China will need energy to do that. So, on the one hand, they don't seek to cut off energy to China, yet there are those in Washington that see war with China as inevitable. Mearsheimer is one of those people that believe China and the US are destined to be adversaries and therefore having the capacity to disrupt the oil flow to China makes good strategic sense.

Keady: Oil prices are currently experiencing dizzy heights – and resources as a whole – is this competition part of that price surge?

MK: The prices of oil are the product of supply and demand – on the demand side everyone wants more oil – Americans, China, India. This is a product of industrialization and the 'automobilism' of the world. Now, the fastest automobile market – India is coming along, so is Brazil, Mexico, and as countries, as people, 'motorize' – that is the term the Department of Energy calls it – the demand for oil is going to rise. So this is hardly surprising. The problem is on the supply side is that supply is not keeping up with demand. This is probably partly geological, that the easiest to find oil has been consumed, and what is left is the harder- to-get oil and not coming on line as rapidly as people would like and, on the other hand, you have political instability in Nigeria, Iraq, Venezuela, and in other oil producing areas that have cut back the available supply. So if you combine rising demand, lack of new sources coming on line and political instability, that produces high prices.

Keady: What about alternatives. Some have discussed that the Chinese are looking at hydrogen and other alternative sources - I know they have a lot of coal. What is your view?

MK: The Chinese have called for the '*study of energy alternatives*' - this is a very recent phenomenon. It's only in the past six months, with preparation of

the 11th five-year plan that began in 2006, that this has become a priority. In the last plan which ran through 2005, the priority was on boosting automobile manufacturing, boosting car ownership, boosting everything for industrial output boosting energy, and there was not much given to energy conservation. This is a very new phenomenon for the Chinese and I think it reflects their sudden awareness that by becoming so dependent on foreign oil, that this is an economic vulnerability and political vulnerability that they had not thought about very seriously, and they are now finding this a real problem so belatedly, they are taking steps. But the emphasis until now has been on selling cars.

Keady: How much oil do they consume?

MK: Right now it is about six and half million barrels per day, which makes them the second biggest consumer, but that is only a third of what the US consumes every day. So they have a long way to go to catch up to the United States.

Keady: Can you shed some light on the attempt by a Chinese firm to purchase UNOCAL – was that a national security matter?

MK: This is a very interesting matter. I believe this to be a turning point in US-China relations. Because what the US has been calling for has been that China become more like 'us' – y'know, capitalistic – to open itself up to free trade, to behave more like any other modern capitalistic country. This has always been the stated goal of the US – so they (China) say.

'Great! We should be able to invest in the United States the way you invest in China – we are all for it – and, hey, here is this company that we want, Unocal Corporation. It looks like a good investment. We'll bid two billion dollars more than Chevron, than American suitor for Unocal.'

Chevron offered 16.5 billion, and SINOOC, the Chinese company, offered 18.5 billion, and if free trade were to prevail, you know – which is the reigning religion of the US, economic religion anyway – UNOCAL should have gone to SINOOC unless Chevron raised its bid. You know that's what Chevron should have done if capitalist rules prevail. That's not what they did. Instead they worked with lawmakers in Washington to try to undermine the Chinese bid by trying to portray this as a national security matter.

Now I think this is partly a combination of just dirty business – you know, Chevron has the co-operation. It so happens the member of Congress representing the district where Chevron is located is the head of the Resources Committee of the House of Representatives. His name is Representative Pombo and he made it his signature effort to defeat SINOOC's purchase of UNOCAL, and he also was a major recipient of funds from Chevron. He may have seen his future – political future - tied up with this. But he was able to organize a campaign to introduce legislation that resulted in the sale of SINOOC blocked on national security grounds in the House of Representatives. And this was inserted into the Energy Policy of 2005, which was passed in August, which made it impossible to acquire UNOCAL.

I would say this was the product of dirty corporate politics on one hand, but also anxiety about the rise of China, and there is anxiety about the rise of China in the United States that is quite emotional and hysterical. Some of it is because China is China and its history – and partly any rising power would threaten American ego; America has an ego problem about surrendering super power status to anybody else – and China is the only contender out there to ever challenge the United States to be number one. And this is deeply disturbing to a lot of Americans, and it is this anxiety, this fear of China that Pombo and his allies in Congress were able to mobilize to defeat SINOOC. This was a completely irrational activity in this sense, in that they claimed that the US would 'lose' all these assets. But the UNOCAL assets are all in Asia, and they were mainly being sold to Asian countries, so there was no loss to the United States of any vital assets, but that is the way it was portrayed.

Keady: Some people said to me that because they were supported by the government, these are, by proxy, government firms, and have an unfair advantage over commercial competitors.

MK: Well, there is probably some truth in that. SINOOC could get low cost loans from government banks, so I guess you would call that an advantage. But anybody who knows anything in the US will tell you that big oil gets mammoth subsidies from the US government, tax breaks, oil from the Gulf of Mexico not paying a penny effectively, so in truth, American companies are just as much served by the government as Chinese companies are. They just won't admit it.

Keady: You've said that disputes over foreign oil will play an increasingly critical role in the US-China relations – eclipsing other concerns such as Taiwan and the bilateral trade imbalance. Is this energy tussle that crucial, Michael?

MK: Yes. I think energy is, because energy is the *Achilles'* heel of American power. America has overwhelming military strength, it has enormous economic power, it's an industrial giant – but it's great Achilles' heel is its dependence on imported oil. If oil were plentiful, if the supply of oil were growing, the United States could rely on nearby friendly countries like Canada and Mexico for all its energy. This wouldn't be problem. But none of those conditions prevail.

Oil is becoming increasingly scarce – with respect to the demand it is likely to become even more scarce, and absolutely as we reach peak oil and the supply begins to contract. So the supply is not ever abundant and it is not available only from nearby countries. More and more of the oil is in areas of the world where the oil is unstable, and anti-American in various ways, because of their imperial past or distrustful of the United States or subject to internal coup d'etats or revolts or ethnic wars. So here you have this powerful USA, and its economy and military, dependent on oil that comes from these overseas dangerous areas, and in which China is also interested for its own reason – not in a competitive sense with the USA, not as part of a strategy of fighting the USA, but because of its own desperate need for energy – is fishing in the same troubled waters, such as Africa and the Middle East and Central Asia.

And so this great *Achilles'* heel mixes or intersects with anxiety about China's rise and China's emergence as a global power. So from this point of view, for Americans this is becoming a serious matter. When the UNOCAL Corporation issue came up in the summer of 2005 – if you read the debates on the floor of Congress, you will see this debate coming up – that the United States is in desperate need of energy, that China is a competitor in areas that we rely on, that China is using methods that we find are unsavory to get its oil. So there really was an expression of concern about China's pursuit of oil around the world – and Congress voted to block China from acquiring this company in direct violation of what every American leader says about free trade. This shows when it was a choice of America's national interest and oil, our security interest trumps free trade and capitalism.

Keady: You talked about the instability of supply. How is this affecting global infrastructure, and transport supply lines for oil? I see that there are a lot of railways that are being built and I wonder if that is about finding alternatives to sea-based transport.

MK: I mean every mode of transport is vulnerable. Tankers are at risk in narrow waterways such as the Malacca Straits – and there is a lot of anxiety being expressed about pirates and terrorists in the Straits of Malacca, Straits of

Hormuz, calling for a naval build up there – and the risk of terrorist bombs, so railroads are at risk as well. So countries are relying on many pipelines. You have greater risk of possible route channels and must devote more and more of the military to pipeline protection, which is what the US is doing all around the world.

Keady: Does this mean, Michael Klare, that alternative sources are on the backburner for the next little while in the Western countries? *‘To hell with it – China is polluting the world – we’ve got to move forward?’*

MK: This, again, is part of the larger march of history, and I cannot just imagine 100 years from now, historians looking at us and saying, *‘What was the matter with those people? Why were they so unable to see the handwriting on the wall, and to shift to adopt new technologies?’* Because I think that is the way it is going to look in retrospect. But right now, we have a whole economic system in this country based on the delivery of oil, to every household in America – every car, every gas station. And it’s the wealthiest economic enterprise in the world, and certainly in the States. So the tremendous incentives in maintaining this system as long as they possibly can – and that essentially was the aim of the National Energy Policy adopted by the Bush administration in 2001– to perpetuate this system another 20 years, that is what it called for. It’s not that they don’t know that alternatives aren’t needed, but they say that for next 20 years, we are going to make this system better and increase reliance on petroleum. This is sort of dysfunctional thinking but it is the nature of human behavior to cling to what is profitable and not make changes that are necessary.

And I see, through history, big coal fought like hell to keep oil taking over coal as the main source of energy and before that, wind. The makers of sailing ships resisted the beginning of steam ships because so many interests were tied up in that. So that is what is happening today – big oil is fighting alternatives but understanding that in another 20 years there will be no choice. But if they can keep it going, that is what they will do.

Keady: Thanks for your time, Michael.

FAREED MOHAMEDI

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MK: Fareed – the National Security Strategy suggested to some a hard line stance against China’s pursuit of energy. Do you think there is competition between China and the US on the energy front?

FM: There are two things. One, the major producers may not be investing sufficiently and, second, there is competition for those supplies and China is definitely coming onto the market.

But you have to put this in the context of another issue, not related to the energy security issue, and that is that the United States feels that – and this has been the policy of Wolfowitz and Cheney going back to the first Bush administration, and in fact the strategic reviews they did back then reflected this sort of thinking – and that is, in 1991 or 1992 they said, ‘We are at a historical crossroads. The Soviet Union has collapsed, we are the sole superpower, and we now can remain the sole superpower forever and a day.’

And who is the only threat on the horizon? And that’s China.

And that policy – in fact they laid it out in 2002, that they are going to prevent China from coming up to superpower status. It can make all the Mickey Mouse watches it wants to, be the economic powerhouse of the world, the industrial powerhouse of the world, but it cannot attain superpower status mainly on the military level.

And the way they wanted to do this is reform the military here, take on certain new threats and all that, but also build the space weaponry. And in space, America would be dominant and that, in a sense, is how they would maintain their sole superpower status. Energy and other issues are subsidiary.

It does come in, in a sense, if they are able to check China’s, or threaten China’s energy security, then China might be more willing to deal with the United States. They have a bargaining chip this way. That’s why the Middle East is important. That is why West Africa is important. That is why they get annoyed

when Chavez talks about diversifying markets and that's where that comes in. The energy part is more tactical, and one way to contain China. The big strategy, however, is to keep China from being a superpower and to keep the US the sole superpower.

MK: So can you tell me what has happened in the Middle East in regard to this?

FM: Some would argue that – *aha* – that is why we went into Iraq, because we want to maintain our supremacy and control over the Persian Gulf because of oil. But I think that is confused. The United States wants to re-organise the Middle East in our own image, to make it safer for our interests. Oil is part of that, but equally or more important is to make it safe for Israel. In fact the crowd that runs the foreign policy are either Israel firsters – or American nationalists.

Cheney, Rumsfeld are the American nationalists that say the only language that the Arabs understand is the big stick, and in that way they identify with the Sharon's of this world that are of the same mentality. Those two have come together to create this foreign policy and Iraq was a part of that. Subsidiary part, and there was some talk of, 'We take control of part of Iraq, make it another Saudia Arabia, then we will diminish the power of that superpower and its oil.' Unfortunately for them, they really screwed it up, but you can say that the control of oil is telegraphed to China. And China – even if the primary objective is not to control the oil to control China, the Chinese think it is. And in that way, they have gone out and reacted and tried to diversify those sources of oil.

MK: So you are saying the Chinese have reacted, decided to diversify their sources of oil. Can you tell me how and where?

FM: First, they want to source oil in the Asia-Pacific area, and you saw that with the gas issue. Second, it's everywhere else: Africa, South America, Canada, so it's all sorts of different sources. Third, Kazakhstan, because it's next door. They want to have a stake in peace and economic stability in Central Asia. Four, Russia. The Chinese do believe that the Russians have strategic envy; as China rises, Russia is envious but, hey, maybe we can do some economic deals and we can get the Russians to play ball with us. The best thing for the Chinese, though, in getting the Russians to play ball, is the way the Americans have taken this unilateralist stance. It's thrown the weaker powers of the world into a passive aggressive stance and they are working together, and one of the ways they are working together is energy.

And then ultimately, and unfortunately for the Chinese, they have to go the Persian Gulf because that's where the oil is, and it's going to be there forever and a day. So then they do deals with Iranians, who are the most reliable as far as they are concerned, and with the Saudis, who they have taken advantage of the post 9/11 diversification of Saudi Arabia's foreign policy, where the Saudi's felt they had too close a relationship with the United States and it was threatening to the royal family of Saudi Arabia. So because of that, Osama Bin Laden said, '*You are in bed with the Yankee imperialists*' and all that, and de-legitimized the ruling family.

In the several months to the Iraq war, the Saudi family had to re-position itself. And one of the ways it re-positioned itself was to say, '*No, we are friendly with the United States. We are also friendly with China,*' and Abdullah went to China just recently. He went to Russia and made a big deal of relations with Putin. So the Chinese have taken advantage of that. But in the back of their minds they still know where the real power lies in the region, and they are very wary of being totally dependent on the Gulf.

MK: We were both at a conference and Robert Ebel talked about the fact that China was responding to the US trying to shore up security of its supply of oil in the region, and in the region in a defensive way. Do you agree with that?

FM: It has no offensive capability. China has no long reach capability. It cannot secure oil coming out of the Gulf, the Persian Gulf, because it just doesn't have the naval capabilities – and it certainly can't do it anywhere else. The Sixth Fleet, by the way, the US Sixth Fleet which patrols the Mediterranean, now makes regular stops in West Africa and is now very much concerned with West African crude coming into the Atlantic and making sure that that just comes out, safe from 'pirates', from 'state failure'. They are afraid Al-Qaeda will get involved ...

MK: But you don't think the Chinese are threatening US supplies...

FM: No. No where in the world – and they do not have the capability.

MK: What about all this talk of submarines and the talk by some in the US that China might threaten US oil supplies by submarines or landmines in the Straits of Malacca?

FM: But they are not US supplies. Where the US can threaten supplies to China, and where China might possibly use its submarines to unblock supplies,

is the Straits of Malacca, or use submarines to secure its defense around its own periphery. The Chinese do not have an offensive capability.

MK: Why have the Indians and other countries been involved in the patrolling of the Straits of Malacca? Is that linked to oil supply?

FM: Well, India has had, for a long time and since Rajiv Gandhi – and Rajiv nearly bankrupted India borrowing money to build up his blue sea navy – so it has been part of its defense posture, vis-à-vis Pakistan, vis-à-vis China, and I think it wants to show that it can play in Asia. I don't see much use in that but that is what the Indian planners are all about.

MK: There was much talk about China raising its influence in Africa and other so called *'failed states'* or problematic states, vulnerable states – you said it was a 'two way street'. You said 'these countries see China as a way of raising their income, of raising their power'. Can you explain this?

FM: A lot of corrupt dictators get a lot of money and football stadiums from Chinese aid. What the Chinese want mainly, to a certain extent, is access to energy. But it is also buying votes for Taiwan, to keep Taiwan out of the UN. So that is a very important element of Chinese foreign policy.

MK: So you are saying the oil and the political are interlinked?

FM: Absolutely. But even if they didn't want the oil, they would build the stadiums, railroads, and pay the dictators because there is the issue of buying votes.

MK: That so many of these countries are so volatile and supply lines so vulnerable – isn't this a problem for the Chinese – and aren't they aware of that?

FM: They worry a lot. I mean, I was in Beijing recently talking to a professor at a university and he was saying that the Chinese leadership worries about this instability, and also worries about its *'reputation risk'* they are associating with these disreputable characters. And they are very intent now on playing a very responsible role at an international level. Having said that, they say, *'What are we to do?'* First, we have to pursue a certain foreign policy because it's a defensive foreign policy, and second, we have to go out and get the energy. So I mean if we can't get it from Saudi Arabia, then we have to go where it is at.

Sudan is one place, or some of the other West African states – we have to deal with difficult people.

MK: Some of the international oil companies – you refer to them as IOC’s – have complained about the way that China has been operating, this call of it being mercantilist – that they are not playing by the rules, that they have a distinct advantage.

Can you tell me: whether you believe it to be mercantilist, but also – what is the difference between the IOC’s and the NOC’s – the National Oil Companies?

FM: Firstly, the oil business is primarily a government business. Seventy-five percent of the oil is controlled by governments, or by national oil companies. So if you want access to that oil, you have to deal with governments. The Western IOC’s have used their governments as much as the Asian NOC’s – the Chinese, the Indians, the Malaysians – have used their governments to try and get access to that oil.

Take Qatar. Even if Mobil (then Mobil before the Exxon Mobil merger) did not bring in the State Department, its government, to prise open the gas sector for itself, the Qatarese certainly thought that by getting Mobil in, they were getting America in. And the Qatar Emir had this plan, of becoming independent from the rest of the region, threatened mainly by Saudi Arabia, but it also wanted to be independent from Iran, because that gas field is shared by Iran. So the Qatari Emir got an American oil company, an American air force base, and Central Command moved there just before the Iraq war. That is our aircraft carrier and our gas field sitting in the middle of Qatar. This is government business! To get access to oil and gas, you need to deal with governments.

So I don’t think that what the Chinese are doing is any different than what the Americans did, what the British did, what the French did with Total and South Paz. When the French put together the South Paz deal they were threatened with sanction from the United States. That deal comprised of Total, Petronas, and Gazprom. One European company - so they got the EU, one Asian company, and one Russian company, to get political cover for itself. So you see how governments are so important.

MK: Well, at the moment the US government is ratcheting up the rhetoric on Iran. Are the energy deals between Iran and China significant in this, and how significant are the deals themselves?

FM: Oh, they are very significant for both countries. Not just in the current stage, but how they grow and develop, because the Chinese companies will be having a bigger and bigger role, I suspect, in Iran.

China has three principles in dealing with Iran: firstly, non-intervention in sovereign states affairs; secondly, ensuring the flow of oil and gas out of the Middle East to maintain the stability of oil and gas markets; and third, it believes there should not be proliferation of nuclear weapons in the Middle East. Two, in a sense, are motivating to check US threats against Iran, and one is a principled position it wants to adopt on a global level, that it doesn't want proliferation, and especially in the Middle East. It has told Iranians, we will protect you as long as you are being reasonable, but if you weaponize, then potentially, all bets are off.

So you see this dual role. China has parochial interests, bilateral interests, but it also wants to play a global geo-political role. It wants to be one of the big boys. And when you play the big game, you have to at least pretend you have certain principled positions. It becomes more and more difficult, especially in a world where the United States, that had at one time played a more principled role in the world, is now playing less of it. It drives others into a passive-aggressive, more defensive posture. This is their aim.

MK: What percentage of Iranian oil goes to China?

FM: Around 14%. That is an important amount of oil... if you don't have that...and the thing is that it is growing. So it's not just the static picture – it's the dynamic picture looking forward. In general though, it's not just about the specific flows from Iran. It's if Irani oil is cut off, then China has go find it somewhere else – and that has an impact on world markets. So that is why one of China's principles is - no blocking of crude or gas supplies coming out.

MK: And is this why there is also this concern from America about Chavez?

FM: What they worry about with Chavez is that he is a trouble- maker in the entire region. That he could undermine US interests in the region. He could 'aid drug dealers'. They make up a lot of things about him. Chavez is playing on the Americans for internal reasons – he also makes up stories about the big bad Americans.

Chavez diversifying is a bit of a pipedream for him – he is very much dependent on the United States, because PDV, the national oil company of Venezuela, owns about two million barrels of captive refined capacity in the United States. And it was a brilliant strategy, PDV in its heyday, a decade and a half ago, to do that, because their crude is very price sensitive so it has to be sold at a huge discount. You face a lot of competition from Middle East suppliers, so if you buy up their refinery, you have a captive customer, and then you can also make the profits downstream.

So they owned the refining and distribution system called Citgo. They are hardwired into the United States. Chavez and his colleagues have always maintained that Citgo was a money- laundering scheme for the last regime, and that we are too dependent on the United States. The US could nationalize Citgo and threaten and blackmail us.

So there is this paranoia that is going on and China is now a way, ‘if we send all our oil to China, then we do not depend on the United States’. But it is extremely difficult to imagine that substantial amounts will go. Firstly because Chavez has been under-investing in his oil sector and production has been falling. So he can barely keep up his supplies to the United States. So let alone meet new demand in China.

Plus there are transport problems. The Panama Canal can only handle a certain size ship going through. The second thing is that he is trying to get the Chinese to build a pipeline along the Panama Canal so it can ship crude. I think it is not really worth it to the Chinese to buy his crude because they would have to spend a lot of money changing their refinery capabilities and capacities at home. There are a lot of technical reasons why a lot of these are rhetorical statements by all sides. Venezuela will remain hardwired into the United States.

MK: You mentioned before we began that maritime security and strength has always been important, and that America really controls that globally. Is that right?

FM: It’s the sole superpower in terms of the navy. Its seven fleets, and one is in Asia, and one is in Europe, one is in San Diego on the other side, so it really can ensure the physical delivery of crude from all parts of the world to its own shores. And it can thwart others and interdict others’ supplies: no-one else can match that.

In that sense, the US has energy security. And of course, the other thing, the US has the capability to invade countries – as we saw in Iraq – although it is a bit constrained right now, but it has the long reach capability to do that. Force projection, as they call it. No other country can really do that.

MK: You mentioned that you don't think Iraq was about oil, but this is what many people believe.

FM: Iraq was about re-making the Middle East in the image of the United States and making it safer for Israel. There was some talk on a subsidiary level that we could make Iraq the new Saudi Arabia, and that would reduce the power of the Saudis. But the primary reason was politics and not economics, and what shocked us was, despite very high oil prices, and despite the threat that high oil prices had to effect the economy, it was willing to invade Iraq. Any time bombs go off in the Persian Gulf, oil jumps ten dollars – and they knew that very well. To hell with economics, it is about acting decisively, and changing the region in our own image.

MK: Well, let's look at the high oil price. Some would say this makes it difficult for China. But are oil imports a significant factor in their economy? And what about coal?

FM: It is significant to this extent: they do subsidies and protect the urban consumer from the real pain of high oil prices, although they are increasingly passing the high oil cost on to the consumer.

But China's growth comes from exports. What it then does, it exports the price of oil. Having said that, the oil price has not contributed to cost push inflation, to higher prices of Chinese goods. Because China has taken a hit somewhere else, it has absorbed it. Because its labor costs are so low, its absorbed it in that sense, or in lower profits. But essentially the cost of oil is exported out to your Mickey Mouse watch. That is then exported out to the rest of the world.

MK: But coal is still the significant energy source, is that correct?

FM: That's the other thing. It has quite a dependence on coal and we, in our projections going out, still believe that China will depend on coal for at least 60% of its energy needs out into the future. The volume of oil and gas will grow, but the proportions will not really change that much in the next twenty/thirty years.

MK: What about the view that they are investing in new technology? How significant do you think this is?

FM: The great issue with China is environmental. If they are going to use coal, they are going to have to invest in a whole heap of new technology – clean coal and all of that. Conservation - because in terms of transport, they are going to have to still rely on oil and liquefied gas to fuel their cars and trucks, which will grow. They are going to have to find new technologies to conserve. So from an environmental and conservation point of view, which ultimately is an energy security issue, they are going to have to invest a lot in new technology.

MK: In Australia – I come from Australia and there have been large gas deals with China on our North-West shelf – if there was conflict with China (and some say it will never happen because of the economic interdependence), are countries like Australia, who is obviously aligned with the US, hedging its security bets? Or should I say, is CHINA hedging its security bets?

FM: The Chinese want to create a web of interdependencies, obviously, but I think the Australians will always maintain a special relationship with the United States, and will be part of any alliance to contain China.

So if gas supplies have to be stopped in case of a war, they will be stopped. And yes, the Australians will lose some money and the private companies will lose money. But we're going into an arena where it's difficult to imagine what happens. A war between the US and China is a BIG DEAL and I don't think we have had a war on that scale for the last fifty/sixty years.

MK: You said at the conference that the administration was one of the most disruptive forces in the oil market. I'd like you to explain that to me.

FM: By threatening Iran, by threatening sanctions on Iran, the US is a) disrupting the flow of investment into Iran b) potentially threatening Iranian oil exports and c) threatening military action against Iran, which is really spooking the oil market. The administration has also disrupted oil flows from Iraq by not adequately protecting their oil sector. It used to produce three million barrels a day, under Saddam at the height of the sanctions, and today it produces two million barrels a day. That's a million barrels off the market. It's got terrible relations with Venezuela, so on several fronts you have this administration disrupting orderly oil markets.

MK: Thanks Fareed. Ω