

Is China A Reliable Stakeholder in Central Asia?

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Thank you very much for the opportunity to appear before you today.

China has a growing presence in Central Asia, but it should not be assumed that their activities in the energy sector will be of direct or even indirect threat to U.S. interests in the region. They are clearly not a direct threat to the U.S. and will only become an indirect threat if U.S. policy-makers decide that they by definition are threatened by any Chinese presence in the Central Asian region.

The authorities in Beijing seem to have been very pragmatic about the independence of the Central Asian countries from the very outset. There is no evidence to suggest that they anticipated the disintegration of the U.S.S.R., and given their own disgruntled Turkic population, there is little reason to believe Beijing thought it was a good thing. But the Chinese leadership and its quasi-state business community have been very pragmatic in establishing and strengthening their relationships with the five Central Asian states, making careful calculation as to China's short, medium and long term interests in the region.

China's short term concerns were initially focused on border delineation issues, and minimizing direct and indirect involvement by the Central Asian states in China's own ethnic minority issues. And China saw issues of long-term economic and security cooperation as being medium and long-term issues, which Beijing authorities would come to address over time.

China has no choice but to view events in Central Asia as having potential direct security impact. China shares a long border with a number of Central Asian states---three in fact---Kazakhstan (which has the longest border with China), Kyrgyzstan, and Tajikistan (with a very small border). By contrast, although Russia's border with

Kazakhstan is longer than China's, that is the only one of the five Central Asian states with which Russia shares a land border; Russia and Turkmenistan have a maritime border in the Caspian Sea. China, of course, also has a vast land border with Russia. When the U.S.S.R. collapsed, the Sino-Soviet border was only partially delineated, and the Shanghai Cooperation Organization, originally known as the Shanghai Five, was established in the mid-1990s as a confidence building measure for what were then newly delineated borders, that now involved five rather than two countries.

The Chinese appeared to have bargained hard to get favorable outcomes during the border negotiations with Kazakhstan and Kyrgyzstan, and at one point Kyrgyz president Askar Akayev even turned over more land than necessary to appease his "thirsty" neighbor (the land in question gave Chinese firm claim to an important water shed). But the Kazakhs and even the Kyrgyz did not come out too badly from this exchange, although critical water usage issues on the Chinese side of the border remain unresolved.

The border delineation went on in an environment of heightened tensions on the Chinese side of their borders with the newly independent Central Asian states. The independence of the Central Asian states had a predictable impact on the aspirations for cultural and national autonomy among China's own Turkic minorities. China's Kazakh and Kyrgyz population were eventually offered limited opportunities to immigrate to newly independent homelands, which dampened, if not eliminated any security threat that they posed. But the challenge posed to Beijing by the Uighurs was far more complex. A much larger ethnic community, they had not achieved any of their political aspirations, and their diaspora community in Central Asia (mainly in Kyrgyzstan and Kazakhstan)

was viewed by the Chinese authorities as potential “fifth columnists” who might destabilize the territorial integrity of China.

In fact, the legal status of Uighur political groups in Central Asia is the one area where Chinese leaders clearly signaled to Central Asian authorities that they would use negative as well as positive incentives to the desired outcome. This led Kyrgyz, Kazakh and Uzbek leaders began to restrict the legal operation of pro-Uighur groups, despite the fact that these groups often engaged some support from the respective Kyrgyz and Kazakh nationalist communities in particular.

Over the last five years, though, China has felt the need to move toward its medium term goals. This is largely the result of the introduction of a U.S. military presence in the region, and the increase in Russia’s economic and security presence in Central Asia. As a result there has been a growing Chinese economic presence in the region, most particularly in the area of energy, and there is a deepening level of security cooperation, largely through the evolving institution of the SCO.

#### China’s Developing Energy Interests in Central Asia

Its basic security issues resolved, China was able to focus more attention to its economic agenda.

China’s size and economic potential make Beijing at least a silent presence in virtually every setting of importance involving the Central Asian states—and sometimes it is a visible and vocal one. Trade with China is increasingly important to all the Central Asian states. Unlike in the first years of independence when much of the commerce was

“shuttle trade”, it is legal trade and investment that is now being encouraged by the various Central Asian governments.

China’s economic presence is largest in Kyrgyzstan and Kazakhstan. Kyrgyzstan hopes to be a gateway to China because they are both members of the WTO. Small and medium sized investors from China are now dominating a number of economic sectors in Kyrgyzstan, especially in the north, and the Chinese represent virtually the only group eager to invest in that small and poor Central Asian country.

More relevant to today’s hearing, China is a major investor in Kazakhstan’s oil industry, as a way to insure increased access to Caspian oil and gas reserves. The Kazakhs and Chinese are building a new jointly owned 2,900-kilometer oil pipeline to which will run from Atyrau through Kenkiyak, on to Kumkol, Atasu, and then Alashankou on the Kazakh-Chinese border. By late 2005 two stretches were already operational. The Chinese National Petroleum Company (CNPC) owns a controlling interest in Aktobemunaigaz, a production company in Western Kazakhstan, but this will not provide enough oil to fill the pipeline, so both the Kazakhs and Chinese are exploring the possibilities of a link with western Siberia, and bringing down Siberian crude.

Chinese ambitions vis a vis Kazakhstan extend a lot further. A 2003 bid China National Offshore Oil Corporation (CNOOC) as well as China Petroleum and Chemical Corporation (Sinopec) to buy British Gas’ share of Kazakhstan’s massive off-shore Kashagan deposit, was blocked by the consortia partners, who in the end were forced to allow Kazakhstan’s own national company (Kazmunaigaz) to acquire half the BG stake, and absorbed the other half themselves. The Chinese remain interested in buying a portion of the Kazmunaigaz stake.

CNPC did manage to acquire the small North Buzachi field, and then finally in 2005 CNPC purchased the assets of PetraKazakhstan, for \$4 billion giving them the assets from the Kumkol field and shared control of the Shymkent refinery (with Kazmunaigaz).

While the Kazakhs sometimes grumble about pressure from China, and the Chinese complain of the bad business practices of their Kazakh partners, the two countries are cementing a longer term relationship. Both realize that the prospect of supplying China could create new synergies between the oil industries of both Kazakhstan and Russia, ones which leave the Kazakhs in particular less vulnerable to non-competitive transport arrangements offered by Russia.

It is less certain whether Chinese plans in Turkmenistan will prove realizable. The Chinese have contracted to begin moving up to 30 bcm of Turkmen gas annually in 2009, through a pipeline which will go through Kazakhstan, linking up with the existing Bukhara-Tashkent-Almaty pipeline and extending it to the border at Alashankou. The Chinese also are negotiating to get Kazakh gas shipped along this route or through a new pipeline from Ishim in Russia, to Astana, through Karaganda and eventually to Alashankou. It is hard to believe the Chinese would support both options simultaneously, and Russia will certainly be lobbying hard for the second route to be built first, as most industry analysts do not believe that Turkmenistan will have enough production to support contract obligations to both Russia and China.

The China National Petroleum Company (CNPC) also signed a \$600 million agreement with Uzbekneftegaz for some 23 smaller oil fields in the Bukhara area. Very little information has been made public about this agreement, but the location of these

fields (near the main gas pipeline) suggests that Beijing is hopeful that there will be large amounts of associated gas available from these projects.

The route of the proposed Chinese gas pipeline will not be finalized until Beijing is confident that Chinese companies have finished cherry-picking available gas projects in Kazakhstan, Turkmenistan and Uzbekistan, with the eventual routing also likely to be designed with an eye of tying up otherwise stranded gas projects to east-west export pipeline routes. This is particularly important for the Uzbeks, many of whose gas fields are now linked only to Central Asian markets.

China too is an interested client for surplus electric power. The Russians are also interested in supplying this market, as are the Kazakhs, who are planning a joint project with China to develop a \$4 billion coal-fired power plant at Ekibastuz, near the Russian-Chinese border. Kyrgyzstan also is interested in selling hydroelectric power to China (which seems more interested in developing its own hydroelectric power than buying foreign-produced electricity).

And in both the Kazakh and Kyrgyz cases the hope is that such purchases might make China less aggressive about diverting upstream water that traditionally flowed into Central Asia. Tajikistan too is attracted by the Chinese market, and even more so by the prospects of exporting surplus energy to Afghanistan, and then on to the large markets in India and Pakistan. The latter route is particularly interesting to U.S. authorities. It would have a developmental impact in Afghanistan and would lead Tajikistan to diversify its resource ownership base beyond Russia.

China's Security Presence

The increased U.S. presence in Central Asia brought Washington's military presence to within a few hundred miles of the Chinese border, and left Beijing feeling that they had to give more thought to protecting their long-term interests in the region. Beijing has focused on bilateral as well as multilateral initiatives. The U.S. military presence in the region has contributed to the strengthening of the Shanghai Cooperation Organization (SCO), of which all the Central Asian states except Turkmenistan are members, as are both Russia and China.

The SCO's first-ever joint military exercises held in the summer of 2003. The SCO Anti-Terrorism Center was opened in January 2004 and formally inaugurated at the SCO head of state meeting held there in June 2004. The Chinese are also pushing hard for bilateral military cooperation with other SCO states, and have made real inroads in this regard with the Kyrgyz, Kazakhs, and most recently and significantly with the Uzbeks. As they do not share a border with China, Tashkent sees only positive aspects to bilateral military cooperation with Beijing.

The SCO has not yet fully evolved as an organization, nor is its final membership set. But with Beijing and Moscow both placing real primacy on an organization in which military and intelligence cooperation is a realistic goal, it seems unlikely that other states will be asked to take full membership any time soon. But observer states like Iran may get a lot of attention, as happened at the 10<sup>th</sup> anniversary summit of the SCO in China in June 2006. This attention certainly suited both Russia and China with regard to their concerns about U.S. policy on Iran, but neither country is likely to sacrifice its longer term strategic advantage in Central Asia by expanding the organization prematurely.



The Chinese expect the SCO to help with energy security vis a vis both Russia and China, and this reason alone talk of expansion would be premature to Beijing. The expansion of the SCO, to try and prevent as well as neutralize future terrorist threats, good bilateral security relations and working to insure friendly regimes come to power in the Central Asian states are all critical to the long-term security of Chinese land-based pipelines through Russia and Central Asia, not to mention Chinese firms maintaining control of oil and gas assets that they have or will purchase.

### Conclusion

China is committed to expanding their presence in Central Asia, and to acquire a substantial stake in the development of Central Asia's hydrocarbon reserves. For China, much like Russia, Central Asian energy resources can make a huge difference in their energy supply, both for domestic use and for export. By contrast, Kazakh oil and Kazakh, Turkmen, and Uzbek gas will only produce marginal improvements in supply for western countries. China, unlike the western countries, is happy to finance improvements in the oil and gas transport system within the Central Asian region itself, and not just potential international export routes. This makes China, a potentially attractive partner for Russia, who lacks the capital to make improvements to the Soviet-era gas transport system through the region, upon which Russia continues to depend in order to make export targets in Europe, money which Gazprom itself now lacks. Moreover, especially given the likelihood that in the medium and long-term Chinese-Central Asian-Russian energy cooperation will increase, there seems little reason to expect the Chinese the Central Asian energy market, no matter how effectively they pursue alternative forms of energy.

From the point of view of U.S. and Western interests more generally, increasing Chinese reliance on Central Asian and Russian reserves (particularly if they are developed in concert with Central Asian reserves) should be a good thing. The U.S. and Western energy companies will remain engaged in the region. China is predominantly buying assets that the West has passed on, and the triangular nature of the relationship with Central Asia, Russia and China will create a fulcrum that minimizes the likelihood that Russia and China will “gang up” against the West in the area of energy security.

It is also not in U.S. interest to try and create chasms in the relationships of the Central Asian states and China. The Kazakhs and the Kyrgyz understand that there is no way that the fate of the future of their countries can be fully separated from that of China. Yet there is little indication that they have become more nervous about China in the past few years. In fact, the opposite seems to be true. Both countries seem a bit more comfortable in their ability to manage this relationship, which they see as sometimes requiring concessions on their part, as was the case with the delineations of borders. But the relationship with China is still more problematic than the one with Russia, because China’s potential power seems almost limitless, and the needs of its growing population could overwhelm those of the Central Asians. For the near term, however, China’s posture toward the Central Asian states seems quite predictable and generally supportive.

For now at least, China is behaving responsibly in Central Asia. If anything they are overpaying to get control of the assets that they desire, and even tolerating asset stripping, which occurred when they lost the refinery to Kazmunaigaz (the Kazakh state oil and Gas Company) that had belonged to PetroKazakhstan at the time of CNPC’s purchase of the company. Obviously, the Central Asians are aware of the fact that there

may be a cost down the road for leaving Beijing frustrated, but for now at least the relationship between these states and China is developing more smoothly than the Central Asians anticipated.

China is also committed to being a source of growing influence in the region, with Beijing confident that the U.S. influence in the region is unlikely to expand significantly, and that Russia's presence will eventually recede, as the Russian state slowly continues to weaken.

China sees itself as an increasingly more active partner for the Central Asian states, but shows no signs that it is likely to substantially increase their pace of growing engagement in the region. They will continue to acquire energy assets and buy up other strategic natural resources and industries should they become available, and with so much surplus capital they are likely to continue to pay top dollar as they do so. Moreover, the Chinese are likely to continue to tolerate bad working conditions---far worse than their Western counterparts would accept---in order to maintain their position in these investments. And they are likely to continue to offer the region's poorer states---Tajikistan, Kyrgyzstan and Uzbekistan---economic loans and loans for the purchase of military equipment. In other words, the Chinese are likely to continue to proceed in Central Asia as they have for the last several years, with a strong sense of confidence that time is on their side, and that they are entering the region to stay.