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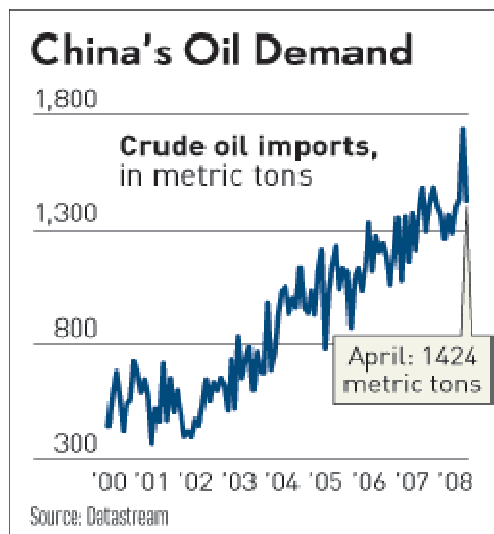
China And Mideast Expand Ties As Oil, Oil Money Seek Homes

By DOUG TSURUOKA

Mideast oil producers are cash-flush with crude over \$130 a barrel. That huge pool of liquidity is increasingly flowing to the world's fastest-growing economy: China.

Some say that could lead to a big shift in global financial power.

In the last year, bankers in Abu Dhabi, Dubai, Saudi Arabia and other Persian Gulf nations have shown a growing interest in investing in China.



"China is going to be a huge consumer of energy in coming decades," said Ted Carpenter, a vice president for defense and foreign policy studies at the Cato Institute. "From a profit-seeking standpoint, it makes sense for Mideast oil producers to develop closer ties."

Kuwait and Saudi firms are building refineries in China. Saudi princes are investing in Chinese hotels. The Kuwaiti Investment Authority was a top investor in the Industrial and Commercial Bank of China's October 2006 IPO.

Meanwhile, a weak dollar is sapping the value of Mideast investments in the U.S. Plowing cash into Chinese assets looks inviting because they promise higher returns in a red-hot economy.

China Craves Crude

Robert Lawrence Kuhn, a senior Citigroup adviser on China, says Chinese officials welcome such interest because the Mideast has what China covets: oil.

"Energy is crucial to China's future," Kuhn said, alluding to growing Chinese efforts to access new supplies of crude.

If China gives greater access to its lucrative markets to nations like Bahrain, it hopes to secure more stable supplies of oil in the future.

Kuhn says China will pay the same market price for oil as others.

"Consistency and robust supply is China's objective, not price advantage," said Kuhn, an investment banker with decades of experience in China and Japan.

Saudi Arabia signed a pact in April 2006 to supply China with a minimum of 1 million barrels per day by 2010 — a 39% jump from 2006.

Such volume agreements are unusual. The Saudis usually prefer to sell oil on the world market on a term and spot contract basis.

Chinese firms also are investing in joint projects in the region to develop oil fields and pipelines that can supply China.

The Chinese are seeking broader economic ties with the Arab world. This includes expanded trade in construction, telecoms and other areas. They're also selling missiles and other military gear to nations like Saudi Arabia.

"China assumes there's going to be a political payoff from these deals as well as an economic one," Cato's Carpenter said.

Two-way trade between the six Gulf states and Asia doubled to \$240 billion from 2000 to 2005, with a hefty chunk coming from Chinese imports and exports.

Underlying China's moves is its ever-growing hunger for oil. It's the No. 2 consumer of crude after the U.S. The Energy Department predicts China's oil imports will catapult by 960% over two decades.

Output from Chinese wells is dwindling. About three-quarters of the nation's energy resources come from coal and natural gas.

"Even if you added up all of China's energy resources, it still wouldn't be sufficient to meet all its industrial needs," Kuhn said.

China's soaring energy demand may be the single biggest reason for oil's multiyear surge, analysts say.


China became a net oil importer in 1993. About 58% comes from the Mideast. Saudi Arabia accounted for 21% of oil imports in 2005.

China became a net gasoline importer for the first time in five years in May. That reflects a surge in cars hitting the road — and refiners cutting output as they face money-losing state-set prices.

Gulf Nations Will Diversify

Kuhn estimates that Gulf nations, including Saudi Arabia, hold about \$1.5 trillion in foreign assets. About 80% is in the U.S., 18% in Europe and 2% in Asia. He notes that by 2009, they're likely to have well over \$2 trillion in foreign assets.

"Over the next five years, you'll see them distributing about a third of their cash in each of these three regions." Kuhn says China will get most of the cash headed for Asia.



Omar bin Sulaiman, governor of the Dubai International Financial Center, said in January 2007 that Gulf banks plan to invest \$250 billion in Asia over five years, with most of it going to China.

China's building its own financial beachheads. In February, the Qatar Financial Center approved the application of ICBC, China's largest lender, to open a branch in the capital, Doha. It was the first time a Chinese bank was allowed to open a branch in the Persian Gulf.

Though China's markets have been hit by a global credit crunch and domestic inflation issues, Kuhn says Mideast investors will still be drawn to Chinese real estate and financial companies.

Nor are Gulf investors leery of putting upward pressure on the yuan with their investments at the expense of dollar-based assets elsewhere. "Mideast China investments would benefit from this yuan appreciation, since it would offset the drop in dollar investments elsewhere," Kuhn said.

Politics Off The Table

Mideast investors relish the fact that China doesn't raise ideological issues like human rights with its trading partners — unlike America. They also aren't keen on big U.S. investments since Congress blocked a Dubai-owned firm from taking over major U.S. port facilities in 2006.

Anne Korin, the director of policy and strategic planning at the Institute for the Analysis of Global Security, sees a darker side to Chinese ties with the Middle East.

"The Chinese align their development aid and foreign policy with their energy needs," Korin said.

She cites China's willingness to use its veto in the U.N. Security Council to shield Sudan and Iran from sanctions. Korin also warns that political factors could weigh more heavily than market ones in future oil shipments.

In Venezuela, President Hugo Chavez is shipping generous supplies of crude to Cuba to tweak the U.S. Back in the 1970s, the Arab oil embargo to protest U.S. support for Israel also was about politics.

Given such precedents, she says it's possible that oil could be used as a political weapon in the future.

"As U.S. relations with the Muslim world continue to deteriorate and we continue to see tightness of supply, we're heading for a situation in a couple of decades where five or six nations in the Middle East control the economic health of the world," Korin said. "China wants to make sure it has strong bilateral relationships with these countries."

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