

Chapter 10

THE GLOBALISATION TRAP

For historical reasons Japan is our biggest importer of energy. But we now want to give preference to China.

Bijan Namdar Zanganeh, Iranian Oil Minister,
on the occasion of the agreement
concerning oil deliveries to the value of over
70 billion US dollars

At the beginning of the twenty-first century the world seems to be turning for China like never before in its history. In this process it is following a logic of integration, which had been brought out by globalisation and skilfully strengthened by the Chinese leadership. The first big surprise of the century was that the world economic crisis drove investors into the Middle Kingdom, as companies are forced to open up new markets and to produce their goods more cheaply. Further surprises were to follow: the Olympic committee entrusted Peking with the most important large-scale event in the world in 2008.

Through the attacks on the World Trade Centre the USA, being the mightiest of China's competitors, suffered the biggest defeat on their own territory in their history. China on the other hand has since then been considered a stronghold of stability, which has made the country more interesting as a location for investment in Asia. The USA was thus forced to change its tone when communicating with China. Within a few days after the September attack Washington redefined the country from being 'a strategic competitor'¹ to being 'a strategic partner'.² China and the USA discovered the common interest of fighting terrorism.

China completed its affiliation with the USA and Russia as space powers with its first manned cosmic flight in October 2003. During the

SARS crisis in the spring of 2003, the leadership showed itself to be slow at first, but then tackled the crisis well, proving that it is able to master domestic disasters competently, and in the process is able to count on the support of its population. The most important change for the future of the world however became visible during the course of the third war in Iraq: one can much more strongly influence the world through economic power than through wars, from which no clear winners can walk away. China is aware of this, whilst the USA still persists with outdated power tactics.

The third Iraq war did also uncover China's vulnerable spots. The battle for the world's energy reserves is becoming harder. China is in a particularly difficult position, as it only has 2 per cent of the world's oil reserves at its disposal on its own territories, whilst China's consumption is rising faster than its state planners could predict. Therefore it has to immediately secure as many energy reserves for itself as possible. Through this it is forced to integrate itself even more strongly with the world. The USA's aggressive policy assisted China in this process. As a result of the mistrust of the world power – the USA – China and most of its smaller neighbours affiliated even more closely with one another than ever before. They mastered their reservation with regards to the new world power, which in return restrained its growing arrogance. The Chinese leadership continued in a disciplined and deliberate manner to change the world according to its plans.

China took a large step in this direction in December 2001 when it became a member of the WTO. Right from the outset it could afford to determine how and when it implemented the agreements that it had made with the world. For a long time China's WTO membership lulled German enterprises into a false sense of security. It is now obvious that the Chinese can continue to determine the speed at which speed it opens which markets. This is because whoever has the monopoly of the future market can repeatedly afford to breach contracts. The WTO membership was the most significant step for China's full integration into the economic world. It was not easy for the Chinese to enter the WTO. Because of the principle of consent they had to reach an agreement with all of the countries about the conditions of entry. On the grounds of the most favoured nation clause they also had to automatically grant the privileges that they allotted to a business partner to all the others. One argued most about which time period and the extent to which the country should open its markets to the world, and vice versa. The most important negotiation partners were the USA, Japan and Europe. And China could negotiate patiently: the longer China waited and the more enterprises produced in China the clearer the balance of power became to

the WTO officials. The barriers to entry that the Chinese establish were to grow over the years rather than shrink. They had not forgotten the trade agreement that had been forced upon them 170 years before by Great Britain, France and the USA and did not want to let themselves to be taken advantage of again.

‘Economical globalisation by no means equals universal harmony’, the former Chinese Foreign Minister Qian Qichen summed up these experiences. ‘Only an armchair strategist would believe in that.’ Long Yongtu, the Chinese head of the negotiations therefore had no reservations in dealing forcefully with the former colonial countries. ‘Negotiating with the Chinese is like hitting a ball against a wall. It rebounds and comes flying back’, admitted EU Trade Commissioner Pascal Lamy.³ The Chinese leadership still has a clear idea of what it needs the WTO for; on the one hand it wants access to the Western markets and on the other it regards membership as an effective means of pressurising its own state enterprises to finally implement reforms. It took nearly fifteen years before China had agreed on all nine hundred pages of text with all of the one hundred and fifty members of the WTO in September 2001.

This step had not been uncontroversial in the CPC. The conservatives had warned that a flood of international competition would destroy millions of Chinese jobs. The supporters, however, gained the upper hand. In order to conclude negotiations Zhu Rongji travelled to the USA in April 1999, in spite of tensions over the Kosovo War. Things did not go altogether smoothly. ‘We had reached agreement when Zhu was in Washington’, recalls former Secretary of Treasury Robert Rubin, ‘But we thought we’d have a better chance with Congress if we’d wait a few weeks to get out of the spotlight. But somehow, to our collective embarrassment, our agreement was leaked on the Internet – we never did figure out how the leak happened, and we certainly didn’t anticipate the reaction in China to the delay in formalizing the agreement. Later in the year, though, Jiang and Clinton had their breakthrough.’ ‘With China’s membership the WTO is taking a big step to really becoming a world trade organisation’, said Mike Moore, the Secretary General of the WTO in a grand statement.⁴ However the event did not release the spontaneous waves of enthusiasm on the streets as the awarding of the Olympic games to Peking in 2008 had done a good two months previously.⁵ In fact this step had a much bigger significance for China and should further increase the scope of the Chinese economy. Later, Jiang Zemin called China’s WTO entry ‘a real test of our learning capacity, our problem-solving, competition, decision-making, and innovative capabilities. In our effort to modernize,’ he used a metaphor from his favourite exercise, ‘we must go swimming in the great ocean of the global

marketplace. 'We must swim – and swim hard – and do everything we can to enhance our ability to struggle with the wind and waves.'

The still-young Chinese WTO history is rather a skilful sealing off than an of integration. Because the industrialised nations need the Chinese market more than the other way round, they hesitate to criticise China's policies and likewise keep their markets closed. Complaints are only carefully formulated: 'the German economy recognises the extent and the speed of the Chinese reform process as a huge accomplishment', stated for example a report of the Asia Pacific Committee of the German Economy for Federal Chancellor Schröder in November 2003. 'Admittedly decisions are still made in China, which either contradict the wording or at least the spirit of the WTO's regulations. Many WTO regulations are only implemented after postponement. (...) The German economy has a great understanding for the phase of difficult restructuring in which China finds itself. However China must also pay attention that German enterprises also encounter increasingly reliable parameters in the difficult environment of the transformation process.'⁶

That WTO members override agreements is nothing new. Even those who have been members for many years protect their markets. In Japan the Western insurance industry has approximately 4 per cent of the market share, even though the country should have opened its markets.⁷ In South Korea not even 1 per cent (of the population) drives imported cars. In 2003 US President Bush protected the American steel industry through tariffs, which were condemned as 'illegal' by the WTO.

What is new however is the extent and the obstinacy with which China deals with the agreements and asserts its own strategy. Also unprecedented is the size of the market and the weak position from which Western countries and enterprises may insist on their rights. If German companies refuse the conditions the Chinese have set, there are at any time French, American or Australian enterprises that agree to them in order to snatch the contract away from the competition. The strategy paper of the German economy which is supposed to, 'accompany China's complete integration into the World Trade Organisation',⁸ basically a document of German powerlessness. The field on which China annuls the rules of the WTO is wide. The Chinese shipping industry is so strongly subsidised by the state that even the German and the South Korean shipping industry are no longer able to face the competition. The Germans reproach the Chinese for the fact that such a policy harms ones own banks and thereby the national budget in the long run. They know this from their own experience: the German shipping industry has been subsidised for years.

Particularly serious is China's handling of intellectual property rights. The registration of patents takes up to two years in China. A period of time

which is more than sufficient for the Chinese industry to copy the product. Even if one has a patent protection on a product, it means very little in China. Theoretically one can in fact sue in cases of theft of technology, but practically the chances of succeeding in such action are very small. It is much more likely that one has to give a precise description of the technical details on the order of the judge in the course of such a procedure, and in so doing one loses further trade secrets to the competition. German mechanical engineering in particular suffers from this problem. For example textile machine manufacturers found copies of their machines in the catalogues of the competitor at a fair in Peking, which included their logo. Some of the machines were even better than the original – the Chinese manufacturers had already developed them further. Usually however the copied machines only deliver 80 per cent of the output of the original, but at 50 per cent of the price. With some German manufacturers the turnover has already halved.⁹ Repeatedly engineers masquerading as customers came to the exhibition booths of German manufacturers in order to uncover further details. Effective international instruments against the theft of intellectual property, such as the so-called enforcement agreements, which file charges in the home country and then enforce the judgements through the authorities of the host country, are not recognised in China, even though although this is customary among the member countries of the WTO. Symptomatic of the handling of conflicts is the argument over Chinese commercial law, which China had to change in the process of its entry to the WTO. When European diplomats saw the first draft in the spring of 2004, three quarters of a year before the introduction of this law, which was to specify the scope for international trading ventures, they could not believe their eyes. ‘This contradicts the agreements of the WTO’, the European Chamber of Commerce raged in an internal report. ‘The market is not being opened, but in fact the opposite, as new and ambiguous regulations are being introduced, which greatly restrict the access to the market.’¹⁰ According to this draft only enterprises that order products that they need themselves were to be allowed to enter without difficulties. The trade for a third party – the norm in trading transactions – was simply declared to be an exception and was not laid down in more detail. Rather the draft comprehensively detailed in which cases the rights of the foreign enterprises were restricted. However procedures for demanding their rights, which were frequently abused by the Chinese competitors and authorities, remained likewise unsettled. After strong diplomatic protest the law was actually partially amended. Adequate legal hold, with which foreign enterprises can protect themselves, is admittedly also missing in the final version that came into force on the 11th of December 2004. Western lawyers are of the opinion that the use of the

WTO regulations for foreign enterprises exists less to guide the opening of new markets and more for the increased planning security for the Chinese economy.

In particular the Chinese export economy profits from the dismantling of quotas and trade restrictions. This situation then also affects Germany where business with China is growing the most. Whilst German exports to the Asia Pacific region only rose by 4 per cent in 2003, the exports to China increased by almost 25 per cent in 2004. With a simultaneous clear increase of German imports at approximately 17 per cent China is consolidating its position as Germany's most important trading partner in the region.¹¹

So that the European market's dependence on Chinese products does not grow too quickly, the European Commission shut a small latch on the Chinese growth pressure in the summer of 2004. For the time being it does not want to grant China the status of a market economy. The import quotas will only fall further when China also continues to further liberalise its market further. Yet China also has enough export possibilities without the concessions of the Europeans.

In the branch of the automobile industry the economic planners in Peking don't even consider it necessary to mask their strategies. 'The Government will continue to control the import of vehicles and protect the local manufacturers with tariff hurdles', said for example Ding Hongxiang, the Deputy Managing Director of the official trading centre for automobile importers, in the presence of the national press agency, six months after China had become a member of the WTO.¹² At approximately at the same time an order was issued to China's automobile importers, that offences against import regulations, which had been committed within the past three years, were fineable with back payments. Soon afterwards a Hong Kong Volvo dealer was slapped with a fine of 9.4 million Euros. The company withdrew from its business in China and the business was subsequently taken over by a native dealer. This sentence was in accordance with Chinese law, but was victimisation nonetheless. This automobile importation business was never established on a legal foundation that would have made it possible for dealers to conduct business legally.

Until 1998 most of the imported cars were purchased abroad in the West and smuggled into the country, after the taxes at the beginning of 1995 had been raised from approximately 80 per cent to 260 per cent. A small car therefore cost 28,000 US dollars instead of 8000 US dollars. In particular the People's Liberation Army earned money from this as the soldiers transported vehicles in their high-speed boats to the southern Chinese coast at night. Around 90 per cent of the Mercedes S classes came into the country in this way, and were thus up to 70 per cent cheaper than a normal tax paid

car. Driving a smuggled car was considered a harmless crime; some owners did not even make the effort of scrapping off the sticker of the car dealership from Miami. The import business certainly had its dangers as the former BMW-China boss, Dong Xianquan got to experienced in 1998. On a journey in his silver grey BMW 740 iL from Peking to the port of Tianjin he was stopped by a police motorcycle patrol. The examination of the chassis number concluded that he was driving in a smuggled car. When he had taken up his new posting at the end of 1997 he had not thought of verifying the legality of his private car.¹³ However in 1998 the then Prime Minister Zhu Rongji, began an anti-corruption campaign that forcefully cracked down on smuggling.¹⁴ But the predicament of the importers hardly improved. Corruption in their sector was to a certain extent restructured by the state and made professional. Instead of suffering from the competition of the smugglers the importers were now forced to operate in a grey area, in which they received import licences from government institutions, which had been granted these by the Ministry of Foreign Trade for their own purposes. The institutions had been strictly forbidden to sell the licences, but for the dealers there was no other way to obtain the import licences. Their price amounted to, depending on the market situation, between 10,000 and 20,000 Euros.¹⁵ As somewhere between 100,000 and 150,000 import licences were issued annually, there was at least a hundred million dollars flowing through the dark system mostly into the black accounts of a group of approximately two dozen state officials and their sponsors. Even today dealers make themselves punishable with every car that they import. Every Porsche, every Mercedes and every other imported vehicle in China has come into the country through illegal business dealings. This is a practical mechanism for the state to control imports and the dealers.

But the state also has a number of variables that change the parameters so that it can regulate the importation of cars. These so-called tariff barriers are regulations that international tariff and customs treaties do not abide by, with which it is nevertheless possible to restrict the market access. So for example only Chinese are permitted to sell vehicles in China; international dealers are shut out or need a Chinese partner. All vehicles have to go through a licensing procedure, in which it is examined if they conform to Chinese specifications and safety regulations. Even German luxury cars need to first undergo a Chinese 50,000 kilometre endurance test and be examined under the exhaust standard 'Euro 1', although all European cars already according to standard fulfil the much stricter criterion of the 'Euro 4'. Again and again vehicles fail the inspection because the Chinese mechanics are not able to operate the high-quality Western testing instruments properly. In addition the

safety regulations require a crash test, which the authorities admittedly often waive and instead resell the car that has been provided under the table. The officials of the authorising agency willingly let themselves be invited to luxurious visits at the parent plants, where they ask inquisitive questions about production speed and work procedures.¹⁶ Occasionally imports are also held at customs for flimsy reasons such as, for example that the wooden boxes in which the cars are packed, need to go into quarantine and be examined for worms. This expenditure squeezes the profits of the dealer's, who with some luxury vehicles have only sold enough cars after a period of two years to cover their expenses of entering the market. And if a new model comes out in the third year they have to tackle the authorisation process right from the beginning. The Chinese government also knows how to steer the market to its own interests without harming the WTO agreements. So for example the WTO requires China to annually make a certain number of new import licences available annually, yet it does not fix, when and according to which criteria they are to be issued to the dealers. Theoretically the Chinese government could award all their import licences within a certain capacity on the last day of a certain year to one single manufacturer. Here too the Chinese are not clear about their strategy: 'China will open the gates to its markets as late as possible. The warehouses are full of cars produced in China', said Ren Qing, the Vice President of the Chinese Trading Centre for the import of vehicles.¹⁷

There is also a prohibition on selling imported vehicles together with locally produced ones. So the manufacturers are forced to establish new trading networks for imported vehicles. This regulation puts the brakes on the sale of imported vehicles and at the same time promotes the Chinese economy in two ways. New sales centres mean both new jobs and also new contracts for the building industry as well as providing an advantage for locally produced vehicles.

If the realisation of large infrastructure projects is being carried through, as for example the construction of power stations or underground railways, then these massive projects are in fact publicly tendered for contract by the Chinese government. Admittedly from the outset it has already been decided – against the WTO agreements – what and how much has to be awarded to local manufacturers. World corporate groups like Siemens therefore only have two possibilities: either they do not sell their products to China or they establish a joint venture company with Chinese manufacturers and risk losing their know-how. With some applications for tender it is even a condition that technology is transferred. German enterprises that operate joint ventures with their own majority, which in the meantime are permitted

in some branches, only get a chance if they hand back the majority that they had so laboriously asserted. Even when the central government wants to ensure that certain standards are adhered to, the provincial governments are inclined to give preferential treatment to their own enterprises.

So too western banks like the Commerzbank or the Deutsche Bank have not gained the access to the market that they expected. Actually the banking sector is supposed to open on a step-by-step basis until the end of 2006. The banks have so far certainly been hindered from doing so. For every branch that a Western bank wants to open in China it has to deposit several million US dollars. If it wants to do business in Chinese currency – and that has to be in their interest – then the requirements are once again raised explicitly. Chinese banks on the other hand do not adhere to internationally accepted regulations. The Bank of International Settlement, residing in Basel, determined in a globally obliging agreement which percentage of their credits the banks have to hold ready as reserves in the case of a crisis. The Chinese, however, ignored this and could not even be sanctioned for it. Western banks on the other hand are only able to sell money in China at certain rates of interest and can only borrow at certain interest rates from the central bank. The margins that result out of purchase and sale are very small. The banks are also not allowed to transfer as much money as they want to China. The Chinese regulators' strategy is obvious: the Western banks should only exercise so much pressure on the Chinese banks through competition, so that they improve, but at the same time do not take any important market shares away from them. The Chinese consider that to be the best way is for the Western banks to purchase expensive minority holdings from the Chinese banks. Firstly the foreigners are never able to influence the business alignment through a minority holding. Secondly they on the grounds of their involvement have to then be interested in feeding the Chinese bank with know-how in order to strengthen their market position. Finally the foreigners make their partner bank more attractive for other investors, if they decide to get in on the act with an initial public offer with 20 per cent in Hong Kong or New York.

The competition among Western banks is so fierce that this system functions brilliantly. The British HSBC was the first bank to join the Bank of Communications in August 2004. It acquired approximately one-fifth of the shares of the fifth largest Chinese banking corporation, which has a market value of 8.8 billion dollars.¹⁸ The HSBC paid the major Chinese bank 1.75 billion dollars for the 19.9 percentage share. It was the biggest foreign investment in the Chinese financial sector. For this the British bank is actually not allowed to take part in decision-making processes but at least grow

along at the same time. The risk that China will be overrun by the West amounts to zero. The Western banks cannot attain any high profits through their business in China, however they do increase their world market share in this sector. It is a deal that works in China's favour, yet it is still one of the best that the banks can close in these difficult times in the world. Admittedly the German banks are no longer financially strong enough to be able to bid in this game.¹⁹

So too the insurance agents, who had already anticipated 1.3 billion new customers, were disappointed by China's WTO membership. Foreign life insurance agents were supposed to be able to operate freely in the Chinese market from the end of 2004, after individual cities and regions had already been opened for foreign enterprises before this date. The implementation of regulations were however delayed to provide a timely advantage for Chinese insurance companies. 'Foreign companies are only allowed into the market, once it has already been bought up', industry representatives complained in a standpoint paper.²⁰ In 2003 the Gerling group had once again withdrawn from its business in China.

China also profits legally from the WTO, at its neighbours' expense. On the 1st of January 2005 trade barriers, that is, quotas in the textile industry were abolished throughout the world. Since then the country, instead of the poorer Asian countries, can produce even more textiles for the world market. The WTO estimates that China's market share in the American clothing industry are likely to shoot from 16 to 50 per cent.²¹ KarstadtQuelle alone increased its imports from China from 37 to 43 per cent in 2005.²² Countries such as Cambodia and Bangladesh are the biggest losers and thus become even more dependant than before on the support of China. For the German customers this is a positive development. There should be a distinct drop in the price of clothes.

China is a developing country that will not let the WTO bring it down on its knees, which is something that will please the critics of globalisation. The country undermines the goal of the WTO, which wants to liberalise trade at any price. It allows itself to place social stability within its own country as a priority. The foundations of the WTO's policy are shaken by this. This is shown by the sobering reactions of the industry representatives in Germany. China justly opposes international economic interests of the West – exactly in the way that the protest movements in the industrialised nations and developing countries have time and again demanded.²³ If there is one country in which the farmers and local businesses do not fall by the wayside in the neo-liberal competition characterised by the West, then it is China. Although there are many who consider the Chinese government to be a regime that shows disregard for its people, it

has pulled more people out of poverty in a short period of time than in any other stage in history. It stands its ground against the economic power politics of the dominant Western industrialised countries. It ensures that capital flows from the First to the Third world, in a volume that has never existed before. Neither the USA nor the UN, nor by any stretch of the imagination the WTO can do anything about this new balance of power. China is too powerful and too successful for them: 'in matters of growth China had the best performance among the large countries and by overcoming the East Asian crisis has proven the best management and ability to react flexibly', Joseph Stiglitz, the winner of the Noble Prize for Economics sums up the situation.²⁴ The country is asserting its national socialism through globalisation.

Just how stable China is in this process showed itself during the global economic crisis at the turn of the millennium, following only a few years after the Asian crisis. After several smaller collapses, the American stock markets suffered its biggest losses between the 12th and 16th of March since the stock market crash of 1929.²⁵ The NASDAQ sank by almost 8 per cent,²⁶ the equivalent of 4.5 billion US dollars, the amount of the entire US American national indebtedness or the combination of Japanese and the South Korean national economy respectively.²⁷ Since its peak in March 2000 it had fallen by 63 per cent. The crisis shook the entire world. For the first time in 25 years the three most important centres of capitalism – the USA, Japan and Western Europe – caved in at the same time. In 2001 economic growth in the European Union only amounted to 1.7 per cent. The number of sold cars in Germany alone sank by 12 per cent. Eight of the nine largest European stock exchange indices sank by more than 12 per cent.

So for the second time after the Asian crisis it showed how clever the Chinese leadership had been not to have lured by the quick money, and so avoided huge foreign debts and short-term credits. Even in the crisis year of 2001 the foreign exchange reserves of over 180 billion US dollars at the time sufficed more than four times to cover the foreign loan commitments for the following year.²⁸ In fact the Chinese stock exchanges had also collapsed, but as the stock markets are not accessible to foreign speculators, it did not result in an outflow of capital.²⁹ China managed to keep the Hong Kong dollar as well as the yuan firmly pegged to the US dollar. Yet the international financial markets still doubted for quite some time whether the country could withstand this much pressure. But in the course of the crisis it turned out that it at least profited as much, as it had been burdened by the crisis. Exports actually shrank, but at the same time more Western and Japanese enterprises were forced to invest there.

Foreign confidence had become a determining factor for China, and it has remains so. The upswing is again reflected in the rental market: while the rents in the top locations picked up by upto 10 per cent, they fell in the rest of Asia by upto 20 per cent.³⁰ China had woken up and was amazingly crisis-resistant.

It is with this certainty that the Chinese government conducts its business. In the autumn of 2002 the party changed its leaders. President Jiang Zemin, who in the confusion of 1989 had begun as a stopgap and had, surprisingly, balanced the conflicting forces skilfully and reliably, passed on the party leadership to Hu Jintao. Deng Xiaoping had chosen him as the best worker of the new generation. In the spring of 2003 the government also changed on a rotational basis. The new government under the leadership of Premier Wen Jiabao surprised their people and the world, in that the policy emphasis changed completely. It was as if the Republicans had been voted out in the USA and the Democrats had come to power. If the old government had been one of the booming cities and rapid economic growth, then the new government stands for their commitment to the interior and social balance. Whilst the booming cities of the east coast had already opened up to the First world, characteristically rural central and western China was as before still deeply stuck in the third as before. Six coastal provinces out of the altogether twenty-two provinces, five autonomous regions and four cities directed by the government produce more than half of the gross national product. 'These are figures that concern me', admitted Premier Wen, 'the development of agriculture and the rural regions is among all issues the most important'.³¹ Also Zhou Xiaochuan the head of the central bank stated, 'We have to adapt our model of development'.³² The model 'growth at any price' with which Deng Xiaoping pushed open the gate to the free market economy has served its purpose. And Peking's mayor explained in a hall full of perplexed Western managers, that 'the social climate is now more important than the investment climate'.³³ After the boom in China and the flow of capital had become a fast-selling item, the time had come to place the economy on a wide, stable foundation. 'Economic growth is important,' stressed vice president Zeng Qinghong, 'but it is not the only criteria for development'.³⁴ The change in policy once again reflected itself in the biographies of the responsible politicians. Before Zhu Rongji came into the central government as the vice prime minister he had been the mayor of Shanghai. Wen Jiabao had ascended from the rural provinces. He was in Gansu for 14 years, where state and party chief Hu Jintao had spent 14 years. He had hardly been in office when he changed its direction. Because the biggest problem of the Chinese upswing lies in the fact that the wealth is developing in the cities, and only slowly trickles through to

the interior. When the deadly lung disease SARS broke out in southern China and threatened to bring the whole country to a standstill, even the usually optimistic analysts of the investment banks saw again a gloomy future of China for the first time since 1989. 'Surely a lot of foreign investment projects will be postponed because of the SARS crisis', thought Andy Xie, Morgan Stanley's Asia economist in Hong Kong.³⁵ Firstly the southern province of Canton was affected, where approximately 480,000 factories in close proximity manufacture and supply the world markets with consumer goods on the Pearl River delta. The virus also brought the economy in the service and the banking sector of Hong Kong to a standstill. In April SARS cases were reported in Peking and Shanghai. 'The world economy which has already been knocked by war and geopolitical uncertainty, could finally be brought to a tilt by SARS', according to Stephen Roach, the chief economist with Morgan Stanley. 'The consequences of the SARS virus focus themselves on Asia – the strongest growth region throughout the world, which up until now has still kept the world economy's head above water.' Huang Yiping, the Asia Pacific economist with Salomon Smith Barney, painted a black picture for China at that time: 'Investors are already considering whether it really is wise to invest so much money in China. I don't think that China will be able to win back, what it has already lost.' The government reacted late, but not too late. Zhang Wenkang, the Minister of Health and Peking's mayor Meng Xuenong were relieved of their posts. Wang Qishan, the provincial governor of Hainan, who had already been Zhu Rongji's problem-solver in Canton, was called to the capital to take over the role of mayor. With strict quarantine regulations and stringent travel restrictions they eventually managed to get the crisis under control – without any noticeable slump in growth.

Next the Chinese government dedicated itself to the great socio-political challenges. According to a study of the OECD approximately half of China's 800 million country dwellers are in fact unemployed; approximately 200 million migratory workers are drawn to the cities as construction workers, waiters or domestic helpers. Corruption and fraud cases fuel impatience. According to Western human rights organisations there are roughly 10,000 demonstrations a year against local governments. The concern is growing that the discontent could reach an uncontrollable scale. Who knows how quickly a cocktail of inflation, unemployment, nepotism and disappointed aspirations can lead to an economic crisis and radical change in the country; the demonstrations of 1989 had resulted under such conditions. Wen Jiabao was formerly the office manager of the liberal Prime Minister Zhao Ziyang, who had opposed the military action and as punishment remains under house arrest to this day.

It is therefore a considerable achievement that Zhao's protégé could go onto become Prime Minister. Eventhough there obviously still is a lot leeway, the most important question is how far can the gap between rich and poor widen, without the social tensions making the country ungovernable? The economy may be bubbling, but must not be left to boil over. So to be on the safe side no matter what happens, the Chinese government makes the effort to dampen the signs of overheating as early as possible.

The eleventh five-year-plan, enacted in March 2005, clearly reflected these concerns. The paper, now called 'program' instead of 'plan', states that it is 'of decisive significance to speed up the adaption to a new model of growth'. The aims are 'sustainable development' and effective macro-economic supervision. Also the programme differs markedly from its predecessors in that it omitted the rigid production guidelines that had been characteristic of the previous plans.

The credit tap was turned off for the urban middle classes as the policy on interest is not yet functional. If at the beginning of 2004 40 per cent of vehicles were being purchased on loans; this was reduced to only 10 per cent by the end of the year. Also homebuyers now have to raise more of their own capital. Yet the farmers got such high wage increases that in the second half of 2004, there were three million unskilled workers missing from the factories in the province of Canton. Whilst the Chinese government openly publicises the changes in social policy, Peking does not exactly tell the world about the reversal of Chinese policy that has a significant impact on the world economy. China is increasingly becoming a raw material world power. One Chinese person actually only consumes about a tenth of the oil as an American,³⁶ but if we look at the total amount of consumption, China has been a heavy weight for quite some time. China already burned more oil than Japan in 2004 and is the second biggest consumer in the world with approximately 10 per cent of global consumption.³⁷ The international Energy Agency (IEA) estimates that global oil consumption will increase by two-thirds up to the year 2030, and that China will already have ascended to being the world's biggest oil consumer in 2020. Even Claude Mandil, the chief of the IEA conceded that, 'China's rising demand for oil was underestimated by our own organisation'.³⁸ 'If China's energy policy does not change radically, its consumption in ten years will lie in the range of 14 million barrels per day', estimates Andy Xie.³⁹

The Chinese government was also surprised by the exploding demand. It was only after the September 11th attacks of 2001 in New York and Washington that the problem suddenly came to light. At first the Chinese leadership was concerned about Muslim minorities, who live in the far

western oil rich area at the border with Kazakhstan and Afghanistan and have time and again rebelled, even though these have not resulted in considerable clashes for quite sometime. But soon it turned out that China had been hit in a much more sensitive spot: it only possesses 2 per cent of the world's oil reserves, and therefore has to import a third of its requirements. 'The September 11th attacks not only affect the price of oil', said Zhu Xingshan, the deputy director of the Chinese Economic Centre for Energy Research. 'China will have to completely reconsider its oil supply and will have to use many different sources, so as to manage the risks.'⁴⁰

Already in 1996 China had begun investing in a three-figure value in billions in oil fields in Sudan, Venezuela, Kazakhstan, Nigeria, Canada and Indonesia. But most importantly the country has been, just like Russia, despite the UN embargo heavily involved in Iraq since 1997, which after Saudi Arabia has the world's second biggest oil reserves at its disposal. Both countries secured themselves oil fields. Even France began to negotiate, but did not complete a deal. Lukoil, Russia's biggest oil company bought a share of the huge west Qurna oil field for 1.2 billion US dollars, whilst the China National Petroleum Corporation and the industrial conglomerate China North Industries Corporation (Norinco), which also manufactures weapons, secured themselves rights at the Ahab oil field located a hundred kilometres west of Baghdad, for a total of 1.2 billion US dollars. In addition the Chinese negotiated over the exploitation of the Halfayah field. In these negotiations China, Russia and Iraq not only had the oil supply in mind, but also the weakening of the American position in this region. To strengthen long-term relations with Iraq, China had comprehensively taken care of the building of infrastructure at the beginning of the nineties, after the second Gulf war. The wording of the Iraq strategy issued by President Jiang Zemin is 'Opposition against the USA without it being clearly noticeable'.⁴¹ Wu Lei, a renowned Chinese specialist for international relations expresses it this way: 'we hardly carry any political baggage. This makes it much easier to expand our influence in the region.'⁴²

China's economic activities in Iraq have not yet been fully grasped. Between fifty and sixty Chinese companies, particularly from the construction and energy sector were involved in Iraq in 2003. The China Machinery & Equipment Import & Export Suzhou Corp. (CMEC), the Shanghai Electric Corp. and the Dongfang Electric Corp had all signed contracts to a value of over 2.5 billion US dollars. The CMEC alone had supplied a power station to the value of 785 million US dollars and had largely finished putting it into place before the beginning of the third Iraq war. First Automotive Works, China's largest automobile manufacturer and VW's partner, delivered buses and pick-ups. In this respect, the American

crusade against terror and the decision to march into Iraq, were very bad news for China indeed.⁴³

The Afghanistan campaign of 2001 had already been a setback for China. The fact that part of the American troops had started the invasion from Mongolia, the buffer state between China and Russia, which had declared itself as neutral, was only a pinprick. That China had already built up very good relations with the Taliban weighed much more heavily on them. Although the United Nations had imposed sanctions against the Taliban, the Chinese state enterprises also involved themselves with the reconstruction of infrastructure in Afghanistan. And so Chinese experts assisted, for example, with the repair of dams and the completely outdated telephone system. 'Only the Chinese are prepared to work under such conditions', said Aryancai Ehsanullah the manager for government contacts with Afghan Wireless Communication Co. in Kabul.⁴⁴ The goal was to combine political and economic interests: China only wanted to become the protective power of countries on their own front door and thereby contain Muslim terrorism, in the neighbouring countries, which threatened western China. And China wanted to secure its supply of raw materials and beyond this to become the raw material hub for Japan and Korea.

When Afghanistan fell into the hands of the Americans the Chinese had to make new arrangements. They concentrated their efforts on Kazakhstan, because the oil-rich country (approximately 6 per cent of the world reserves) shares a 30-kilometre border with China and stretches up to the Caspian Sea in the east. So, the ideal area for a Chinese pipeline. Therefore Hu Jintao's first overseas trip in May 2003 also brought him to a country with 14 million inhabitants, carrying 800 million US dollars in his luggage.⁴⁵ A joint venture between the Kazakhstanis and the Chinese had already been extracting oil in Kazakhstan for a considerable period of time. As early as 1997, Kazakhstan's Head of State Nazarbayev and Chinese Prime Minister Li Peng signed a treaty concerning what was then China's largest foreign investment, altogether 9.5 billion US dollars.

Likewise in 2003/2004 China began the construction of a 4000 kilometre pipeline, costing 20 billion Euros, from the western Chinese province of Xinjiang to Shanghai, which will connect central Asia with the booming coastal region. Since the nineties Peking had also endeavoured to stabilise the economy in the other central Asian countries. In Uzbekistan China helped with the building of a railway. It is for this reason that in the summer of 2001 the Peking leadership had, still before the attacks, founded the 'Shanghai Six' together with Russia, Kazakhstan, Tajikistan, Kurdistan and Uzbekistan – an international alliance against terror and separatism. For the first time China tried to visibly position itself as a political player in the region. At first this

alliance was smiled upon condescendingly by the USA. After September 11th 2001 the co-operation suddenly gained significance.

Months before the third war in Iraq, China and Russia started to worry about their investments in Iraq. Whilst China was outwardly quiet the Russians did not mince their words. A top Russian manager from the oil industry said that China and Russia were both intervening behind the scenes with the US government, and that they would come to an agreement on the occasion of President Vladimir Putin's visit to Peking in December 2002.⁴⁶ The Americans reacted severely to the attempt to undermine their power in the region. They had just occupied Iraq when Thamer Ghadhban, who had been appointed as the Iraqi oil minister by the Americans, announced to the *Wall Street Journal* that the contract with China over the exploitation of the al-Ahdad oil field was, 'mutually agreed to be no longer valid'.⁴⁷ The president of the China National Oil and Gas Exploration & Development Corp. (CNODC), Wang Shangli countered that 'this is news for us. Ghadhban was only recently appointed. He doesn't know us at all'.⁴⁸ According to lawyers the contract for the oil field holding up to 1.5 billion barrels is as stated by international law still legal: 'The Republic of Iraq continues to exist, and thereby also its institutions.'⁴⁹ But China preferred not to settle the conflict in public.

For China the third Iraq war was probably the hardest set back in the short history of reintegration into the world economy. There are a few reasons to believe that this will not be the last dispute between China and America over mineral resources. The third Iraq war will possibly go down in history not as the 'clash of civilisations' but as the first Chinese American conflict over the world's oil reserves. To secure the American way of life, the government in Washington was prepared to strain their international relations to the limit and to sacrifice the spilling of a great deal of American blood.⁵⁰

The new competition in the Middle East was just as dangerous for the USA as the threat by Saddam Hussein. The biggest problem is the USA's alliance with Saudi Arabia, the world's biggest oil producer. Its arch-conservative leadership supports both the USA and Arab terrorists. The American oil industry⁵¹ and probably the political hawks pointed out to the government on several occasions that the following scenario was impending: Energy hungry China could go into a similar functional alliance with Iraq, the second most important oil producing country. This would be easily materialised, because the Iraqis and the Chinese are closer politically, than the USA and the Saudis could ever be. And both would be of enormous mutual benefit: China could secure itself parts of the second largest oil fields of the world and Iraq would have a major client, who would not be

concerned what kind of regime was in power in Baghdad. 'China has little room for morality', a Foreign Affairs article informed its readers because one pillar of Chinese diplomacy is that one does not interfere in the internal affairs of other nations. Iraq would also have the opportunity of obtaining ballistic weapons from China, which hardly any other country would sell to them. The USA would then depend more on the Saudis than ever before. If this alliance should falter, Washington would no longer have a new 'partner' in the region. The USA therefore had to act quickly. The fight against terrorism was a welcome cause, to free itself from this geopolitical defensive. Even Donald Rumsfeld, the US Secretary of Defence eventually conceded that there was no connection between the invasion of Iraq and the attacks on New York's World Trade Centre.

The Chinese government however had no interest in drawing the world's attention to their weaknesses. They did not show their anger outwardly, particularly since a public protest would have raised the unpleasant question about why China had not complied with the embargo. Now the country certainly had to look for new ways to secure its source of energy. Originally Peking had wanted to slowly and inconspicuously build up its oil reserves. But now the supply situation had become uncertain, the price threatened to rise. They immediately began to stock up their reserves. Before the Iraq war China was content with having sufficient stocks in order to be able to supply the country for 35 days, although Western countries install reserves for 90 days and Japan even for 120 days. 'The Chinese demand is the driving force behind the rising world wide demand', is how a report of the IEA in Paris summarised the situation. In 2004 alone the price of oil rose by 40 per cent, and put the level of worldwide economic activity, including the German, under enormous pressure. *The Economist* dubbed China the 'hungry dragon'⁵² on its front page, and the ZDF (a German television channel) commented: 'China with its enormous growth potential and associated high consumption of raw materials is booming to extent that it threatens to become a global problem. In the entire industrialised world the oil supply is strained. This is not only the cause of the threat of terror from al-Qaida or the situation in Iraq.'⁵³ China already needs as much oil as Saudi Arabia, Kuwait and Iran produce together.

China is not only buying oil, but is also securing itself other raw material deposits in far off lands. Beside natural gas, these consist of iron ore and copper and most importantly bauxite, which is indispensable for steel smelting, as well as tin needed for the manufacture of tin plate (i.e., cans), plant protection agents and paints. China is currently the world champion in tin consumption, because the booming electrical industry uses it as tin solder. Copper, which is processed, among other things in cables

and washing machines, costs approximately 70 per cent more in 2004 than it did in 2003.⁵⁴ Nickel that mainly serves the purpose of steel refinement costs about 50 per cent more in 2004 than it did in 2003. Gold and platinum increased by around 15 per cent. In 2004 the CRB index which indicates the future prices of 17 raw materials, reached the highest level in 23 years.⁵⁵ China accounts for approximately a third of the worldwide ore imports and is thereby the biggest importer in the world. However at present the Chinese annually use only 200 kilograms per head, whilst the South Koreans are already at the thousand-kilogram mark.⁵⁶ In 2003 China consumed, with 257 million tons, a quarter of the global steel production. It was thus the first country that produced more than 200 million tons of steel annually. This accounted for 23 per cent of the world's production and was higher than the production, which the two greatest economic powers, the USA and Japan manufactured together. In 2004 alone China added on over 20 per cent and thus accounted for almost a half of world's growth in production. At the same time period China used 40 per cent of the worldwide coal production and processed 25 per cent of the steel production. 'The supply can not keep up with the rising demand', said Klaus Matthies, the raw material expert with Hamburg's World Economic Archives (HWEA).⁵⁷

The Chinese government was hardly prepared for this growth. In 2000 it had forecast a steel production of only 140 million tons in the five-year plan. Investments in the steel sector thereupon rose by 96.6 per cent in 2003, and in the first quarter of 2004 by 106.4 per cent. Worldwide, Germany lies in sixth place with nearly 45 million tons of raw steel, behind China, Japan, the USA, Russia and South Korea. By 2007 China wants to have overtaken Europe as the world's biggest producer of high grade steel. 'This is realistic', says Albrecht Kormann, the managing director of Dusseldorf's steel trade association.

This rapid ascent China has created steel producers who are able to compete with the producers of the world's first league. The largest enterprise is the Baoshan Iron & Steel (Baosteel). In 2003 the group with 100,000 employees had a turnover of 14 billion US dollars, with which Baosteel ascended into the list of the 500 largest enterprises in the world. The enterprise managed to rake in 1.6 billion dollars profit – a rate of 14 per cent profit, which presented the Baosteel share being traded in Shanghai with a growth rate of 70 per cent. In China the enterprise has a market share of 10 per cent. Fourteen per cent of the steel is imported, particularly expensive high-grade steel. But China wants to turn the tables and become a steel exporter within the shortest time possible.

The German steel industry underestimated the steel boom. 'We simply knew too little about the expansion plans of the Chinese', said Dieter

Ameling the president of the steel trade association. It was for this reason that the German capacities were not expanded. Whilst the world's steel production rose by a good 9 per cent in 2004, it only grew by 3 per cent in Germany.⁵⁸ For example in 2004 the German steel manufacturer Salzgitter AG was barely able to reach 2001's record gain. The ThyssenKrupp AG regards the developments in the steel market with mixed feelings: on the one hand the group's order books are filled because of the high demand; on the other hand the high cost of raw materials cannot be completely passed on to the customers. 'Those who believe that this development will once again disappear like a ghostly apparition, and that raw materials and steel will soon be available in abundance, are mistaken', said Benedikt Niemeyer the managing director of the medium-sized enterprise Schmolz and Bickenbach AG in Dusseldorf.⁵⁹

In view of the rising steel prices even steel scrap iron has become a rare and therefore valuable commodity. In 2004 the price rose by 145 per cent. Whereas a few years ago one still had to pay at least 100 Euros on a German scrap yard in order to get rid of one's old car, nowadays the scrap dealers pay you 100 Euros for it. Only in this respect does China's bulk buying have a positive effect for the German consumers. The German metal industry already complained to Federal Chancellor Schroeder in 2003, before his trip to Peking. The state gave back turnover tax to Chinese enterprises if they bought Vorstoffe and scrap iron for the non-metal industry and steel scrap metal. Because the market is bare, the German industry has to process expensive premium material or reduce capacities.

The strain on the level of economic activity through the rising price of raw materials is also reflected in the financial markets. The rough direction has been indicated for some years: the dollar is falling and the Euro is rising. A few days after George W. Bush's re-election in November 2004 the dollar fell to its historical provisional low of 1.30 against the Euro. Although the budget deficit turned out to be less than what was at first expected, the American economy was unable to give its own currency any momentum. Under this pressure the European currency had already uncoupled itself from its economy. The Euro is too strong for the weak economic growth in Euro country. The fate of the world's leading currency increasingly lies in Asia, and especially in China, which has through the demand-dependent oil price, the pegging to the US dollar and its foreign exchange reserves, a substantial influence on the development of the rates. A country such as Germany, which almost lives only from its exports only, is particularly susceptible to fluctuations that in Asia. It appears that China's shopping list for raw materials will in future decide the scope of Germany's level of economic activity. The USA's economic activity (Germany's biggest

export customer) will increasingly experience difficulties, because everything will become more expensive in the long run. There is no change in this trend on the horizon. Increasing numbers of investors on the international financial markets, and especially in London, have speculated on this scenario since the second half of 2004.⁶⁰ They gain if the US dollar depreciates, and thereby put the American currency under additional pressure.

But does the scarcity of resources not strangle the Chinese economy also? Just like other countries the giant realm also has to pay a great deal for its mineral resources on the world market. For years now China has been suffering from an energy shortage. The coal-based electricity network reached its limits long ago. For several years there have been power cuts during the summer in the factories of Shanghai and the southern Chinese boom regions, which sometimes last for days. In fact it will only be possible to get the energy problems under control by the end of the decade at the earliest, when China can put a number of new nuclear power plants and more modern coal-fired power stations into operation. But even today the worldwide raw material crisis is more of benefit to China than of harm. The Peking leadership has learned how to exploit the problems of the developed countries for its own purposes. Because less is being bought throughout the world during the crisis, the producers have to increasingly manufacture more cheaply. There is no country that can profit more from this than China.

The investment bank Goldman Sachs takes the view that we are only at the beginning of a cycle, which could take five to ten years. This time period is necessary to build the infrastructure with which one exploits the new mineral resources. At any rate China has reserve levers at its disposal with which it can cushion surprises. The foreign exchange reserves of over 520 billion US dollars work like an insurance, as China can influence the economic situation of its most important trading partners by switching into Euro, yen or US dollars.⁶¹ The pegging of the yuan to the US dollar also functions as an emergency valve, with which China – if necessary within minutes – can take the pressure off the US dollar. In order to decrease the dependence on the USA, China is increasingly turning to its neighbours. It conducts its foreign policy in the inconspicuous garb of a trader. It does not wrestle with its distrustful neighbours on the grounds of political strategies, but instead offers them business deals, which are very attractive for both sides. China assists Kazakhstan, Vietnam, Mongolia, Laos or Thailand with infrastructure and technology transfer for the development of their economies, and instead buys expensive raw materials. With this pact the region is after the same thing. Because the more difficult it gets to deal with the Americans, the more interesting the Chinese offer becomes.

The fact that Kazakhstan has registered the biggest new oil and gas finds in the last few years has proved itself to be very fortunate for China. The ninth largest country in the world in terms of its land area, yet with fewer inhabitants than Peking, possesses – according to its own data – approximately 4 billion barrels, and there are assumed to be at least a further three to four deposits of such volume. At present it has a nearly 7 per cent share of world production. It has very good oil at its disposal, added to which it is difficult to extract. With every dollar that the oil price increases it stands to gain.

Shortly before the outbreak of the third Iraq war the China National Offshore Oil Corp. (CNOOC) and Sinopec bought, within a period of a few days, altogether for 1.23 billion US dollars a 16 per cent share of one of the biggest oil and gas fields that have been found in the last 30 years, from the British BP group. A good 6 months before that China had already secured itself shares of reserves in Australia and Indonesia for 1.1 billion dollars as well as shares of an Algerian oil field for nearly 40 billion US dollars. Never before had the country acquired such huge fields in such a short of time. The CNN tv channel even spoke of ‘aggressive’ buying. The fact that Chinese firms were regularly outbidding Indian companies in the Middle East, in Africa and in the Caspian region led to tensions between the two great powers from Asia. On 12 January 2006, however, the two governments sealed an agreement over closed communication with regard to their planned bids.

With the acquisition in the Caspian Sea, CNOOC joined an already ongoing project belonging to an exclusive consortium. ExxonMobil, Royal Dutch Shell and Total each own the same amount of shares in the lucrative field. Production is set to begin in 2006.⁶² The future plans of the international corporate groups are being foreshadowed. The oil giant Chevron Texaco alone wants to invest 4 billion US dollars in Kazakhstan over the next four years. ExxonMobil is even talking about 40 to 60 million in the next 50 years.⁶³

In May 2004 China and Kazakhstan signed a contract for the construction of an oil pipeline over the Kazakhstani-Chinese border. Construction was carried out with Chinese momentum; building started in August 2004. The China National Petroleum Corp. (CNPC) and the Kazakhstani oil group Kazmunaigaz want to have the 1240 kilometre stretch operational at the end of 2005. Its capacity is to be gradually doubled from a start of 10 million to 20 million barrels. Additionally CNPC is investing in the exploitation of oil and gas deposits in the Caspian continental shelf. Since September 2004 a new section of a pipeline from the Caspian Sea to China has been under construction. The 988 kilometre long section between the Kazakh oil

terminal Atasu and the Chinese railroad-hub of Alashankou is scheduled to go on-line in 2008. The extremely expensive pipeline is expected to cost more than four billion US dollars, and with its capacity of 10 million tons per year will supply only an estimated 4 per cent of the Chinese import demand at initial operations in 2008.

Nevertheless Nursultan Nasarbajew, the president of Kazakhstan is keeping all his options open and does not lean towards Russia or China or even the USA. 'We are trying to maintain a good relationship with all three and therefore would like our pipelines to go in as many different directions as possible', he said in November 2003, 'we have a good relationship with Russia. We are currently building a big pipeline to China. We are very grateful to the Americans for their investments, and for the fact that they have driven the Taliban out of Afghanistan. We support the United States with the building up of Iraq. We believe that in the end Iraq must solve its problems by itself.'⁶⁴ The Chinese however have the crucial advantage that they can support Kazakhstan with the aim of developing it up into the Saudi Arabia of Central Asia. As an ascending world power they are more calm and collected than the USA, which as a declining world power, wants to gain influence at almost any price. And the Kazakhstanis do not have to overcome a difficult past with the Chinese as for example with Russia, whose government to this day have little confidence in the region. 'The Chinese don't want to improve the world. They want to do business', was the point made by Grigori Marchenko, the former head of the central bank and current vice prime minister.⁶⁵ And it is exactly in this matter that one no longer believes the USA.

Even Vietnam with its 82 million inhabitants, now has to rub shoulders with its unloved neighbour. With an annual income of 480 US dollars per head, which does not match half of the Chinese income, Vietnam has no other choice but to attach itself to the upswing of the big neighbouring country. This is despite the fact that the two communist countries have for decades been fighting like cats and dogs and have a thousand-year-old history of enmity. Vietnam needs China's help for a lasting development – and will have to pay for this with its most expensive commodity: with mineral resources. Vietnam is Asia's only net exporter of energy resources and food. 'We are not afraid of China', said Prime Minister Phan Van Khai. 'China is a great country. China's competitive ability in the world looks for its own kind, and the country is a huge market for Vietnamese exports. China urgently needs our raw materials in particular.'⁶⁶ Vietnam and China are negotiating over a joint venture for the extraction of bauxite. Approximately two billion US dollars need to be invested. They are already discussing co-operation within the oil industry. In return Vietnam

is dependent on imports from China's industry. Televisions, refrigerators and countless motorbikes come predominantly from China. 'Our population is benefiting from these cheap products', remarked Prime Minister Phan. Labour costs are actually lower in Vietnam, but international investors nevertheless prefer China. The furniture house Ikea made the calculation with the sample of a new metal folding chair. The pure production costs were in fact around 15 per cent cheaper; however if one includes containers, authorisation and telephone costs, then the calculation came out in the favour of China.

Thailand's relationship with China is also changing due to pressure brought on by global changes. Whilst the USA is becoming increasingly less attractive as a partner, as they stir up the hatred of the Muslim minority in the south of the country, China becomes more interesting. The outcome of a survey conducted at the end of 2003 was that 76 per cent of Thais regard China as their closest friend and ally, whilst only 9 per cent consider themselves to be united with the USA. Ten years ago it was exactly the other round. 'China is making us stronger, because we take on the competition', explained the Thai Prime Minister Thaksin Shinawatra in March 2004. 'We certainly cannot defy China in that we become even cheaper. We have to find our niche instead'.⁶⁷ Logistical co-operation in the energy sector is considered to be one of these. In 2003 the two countries agreed upon the construction of a pipeline through the 400 kilometre wide isthmus between the Andaman Sea and the Gulf of Thailand. Thereby the oil can get to East Asia both more quickly and safely compared to the long route taken by tankers through the straits of Malacca between Indonesia and Malaysia.⁶⁸ In addition China began to establish oil storage facilities along the pipeline in 2004. China's reserves are to be spread out in different locations for safety reasons.

Mongolia is in a similar way increasingly coming under China's sphere of influence. Whilst the Americans are interested in the country as a strategic base, and a traditional bond exists with Russia, China is again the country's best customer. The Chinese are not only interested in mutton and Kashmir wool, but also in Mongolian copper. In 2003 Mongolia discovered the biggest copper deposits that have ever been found in the world. In the same year Chinese President Hu travelled to the capital city of Ulan Bator, bringing with him 300 million US dollars in development aid. From 2006 onwards the new mine will extract copper and also gold to the value of at least 60 billion US dollars.⁶⁹

Even the hermetic North Korea is being swept along by the global demand for mineral resources. It is not only because the Stalinist country represents a risk for the security of the region, but also because it is loaded up to the brim with mineral resources, that China, Russia and the USA are

striving to integrate it into the world for their benefits. North Korea possesses hard coal and 43 other minerals, which are becoming increasingly valuable and is already the second biggest magnesium extractor. It is in a political situation similar to the one China was in at the end of the Cultural Revolution. Whenever it does take place, the opening of North Korea will represent an enormous economic profit for China. In 2003 the trade between China and North Korea amounted to approximately a billion US dollars, a growth of 46 per cent, of which minerals and metals are the largest share. In return the North Koreans receive oil, agricultural products, simple consumer goods and assistance with the construction of infrastructure.

China is also securing sources of raw materials for itself outside of Asia. Because the Chinese commit themselves to long-term contracts at a good price, the Australian corporate group BHP Billiton, one of the biggest enterprises in the world, took up a national Chinese steel group as a partner for the first time, for a 40 per cent share of a new ore mine in 2004. Additionally ore delivery contracts were signed to the value of 12 billion dollars. Half of the future sales volume of BHP's nickel production was likewise sold to China. The enterprise showed with 3.4 billion US dollars for the financial year 2003/2004, the highest profit that has ever been brought in by an Australian company.

China invested a billion US dollars in a bauxite-aluminium complex in Brazil, and between 5 and 13 billion US dollars in steel plants, gas pipelines as well as in iron and uranium mining; 440 million US dollars in India for the production of aluminium; 500 million for copper extraction in Chile; 650 million US dollars for a 85 per cent share of a nickel field in Papua New Guinea.⁷⁰ In Argentina China will invest 15 to 20 billion US dollars in the next few years into oil production before the coast of Patagonia, as well as in iron ore mining and in the railway network. In Brazil it will invest 5 to 13 billion US dollars into steel plants, aluminium-smelting works, gas pipelines and into iron and uranium mining. Three billion dollars flowed to Chile for the development of copper mines and to Venezuela at least a billion into oil production, gas pipelines, refineries and gold mines.

In November 2004 President Hu Jintao and a delegation of 500 managers spent two weeks travelling through South America. In the last days of that year the Venezuelan President Hugo Chavez and the Chinese government agreed that the Chinese would be allowed to develop 15 oil fields and also set up a refinery there. The contracts were at the expense of the USA, who until now has bought 60 per cent of Venezuela's oil.⁷¹ It is above all because of China that South America once again has a current account surplus for the first time in ten years.⁷²

China is increasing its activities in Africa as well. Foreign minister Li Zhaoxing visited six African nations between 11 and 19 January including Nigeria, Libya, Senegal and Mali. In the last two years alone more than 100 meetings between ranking Chinese and African officials and business people have taken place. The fact that Peking issued political guidelines for its Africa policy in January 2006 for the first time is a further indicator of China's increased interest in Africa.

Japan and Korea, which until now were the most powerful countries in Asia, are not only forced to fight against China for their share of the world's mineral resources. They are also drawn into an ever-increasing dependence on the country, because their commercial streams are shifting in China's direction. In 2004 the trade between Japan, China and South Korea constituted a volume of two trillion US dollars – a third of the total trade of the three countries. Particularly the Japanese economy, which has stagnated since the beginning of the nineties, owes its recent recovery to Chinese demand. Whilst exports to China rose dramatically, they have shrunk in the rest of the world. Added to this are the profits that the Japanese companies make with their products manufactured in China.

South Korea, which is the eleventh largest economy in the world, has a similar experience. Already in 2003 more Korean goods were exported to China than to the USA for the first time. Together with Hong Kong, China absorbs a quarter of South Korean exports. Approximately 20 per cent of the growth of about 6 per cent is on account of China. China will attempt to relegate the American influence in Asia to the fringe. Those realists who acknowledge that states do not have to strive continuously for maximal power but rather be able to secure their own security by less offensive means are leaning towards a less pessimistic view on the future of Sino-American relationships.

The trend of the greater integration of Asia, however, works in China's favour. In 2004 the exchange of goods among ASEAN countries grew by more than a third; the volume reached the hundred billion US dollar mark. Starting from 2005 China will be a more important trading partner for the Asian countries than the USA. Therefore it is of greater importance for the states of the region to support China, than to promote the American's consumer level through certificates of indebtedness. Asian unity is accelerated through the ASEAN free trade agreements that were reached in November 2004, which are to eliminate all tariffs up to 2010. Additionally the ASEAN countries recognised China as having the status of a market economy. On this occasion Premier Wen did not want to leave it to the quiet political tones, with which the Chinese otherwise tend to move around in

Asia, and spoke of an 'all encompassing strategic partnership for peace and prosperity'⁷³ in Asia. The USA tried to use its political weight to disrupt this unity. They had been successful with this once before: Japan wanted to set up an Asian monetary fund in 1997, but had to put the plan on hold under the pressure from Washington. Nowadays the USA is no longer powerful enough to be able to do this.

One way to deal with this is further integration of China; the other is containment. This second prong of American strategy amounts to building and increasing co-operation on security issues with various nations in China's neighbourhood. The tightening of American security networks in the region is certainly not solely – and, as far as the public is concerned, not predominantly – motivated by concerns with regard to China. Singapore is increasingly co-operating with America in the field of security policy; Thailand and the Philippines were granted the status of 'major non-NATO allies'. The following initiatives made last year belong in the same context:

- a new security agreement with Japan concerning the deployment of an aircraft carrier and Patriot-missile defence systems (in February 2005, moreover, the American–Japanese alliance for the first time referred explicitly to the security of the Taiwan Straits in a joint address);
- an agreement with India on co-operation concerning civil nuclear technology, aerospace industry, and relaxation of restrictions on arms sales;
- an agreement concerning the admission of Vietnamese soldiers in an American training-programme;
- the re-establishment of co-operation with the Indonesian military and the lifting of all sanctions on arms-sales that had been imposed with regard to human rights concerns;
- the first visit of an American president to Mongolia, military aid (an annual US\$ 20 million) for the modernization of the Mongolian army and joint Mongolian-American military exercises designed to reach interoperability during peace-keeping missions.

In view of the uncertainties in consequence of the rise of China as an emerging power, the two-pronged American strategy is a rational approach. It seems to enjoy a broad consensus within the administration. And in the wider public the Bush administration's China policy has hardly been contested. The reasons for this are as follows:

- After China has been granted regular trading status at the end of Clinton's presidency in 2000, the annual decision concerning the extension of the

most favoured nation treatment were dispensed with. Consequentially, China-critical lobbyists and members of Congress lost their central instrument to influence the public debate.

- President Bush's policy to beef up support for Taiwan while simultaneously warning Taipei not to alter the island's political status stole the influential Taiwan lobby's thunder.
- Finally, the 'war on terror' caused other issues to take a back seat – including China. The 'united government' approach may have further subdued the profile of Congress.

In the two remaining years of the Bush administration, America's China policy may move up the agenda and become increasingly contested. Two reasons support this view:

- There are a number of strains on economic relations, such as a growing deficit, the insufficient protection of copyrights, trade barriers and Chinese monetary policy. The American business world seems to be far less supportive of a policy that is intensifying China's integration than it has been in the nineties; small- and medium-sized companies are particularly worried about Chinese competitors and copy-cats; large enterprises, the driving force behind American business activity in China, are anxiously wondering whether China will ever accept open markets.
- The global expansion of China's economic and political influence, as well as the fierce competition of natural resources and Chinese efforts to modernize its military provide a sounding board for those who wish to see containment on the top of agenda in America's China policy. The strong response in Congress to the proposed acquisition of Uncoal – certainly no heavy weight among American energy-firms – by a subsidiary of the government-owned Chinese oil company CNOOC shows how sensitive the issue of supposed threats to American national security is.

Yet, as long as the administration shows a consistent approach in its China policy, substantial challenges by Congress remain unlikely. Should the constellation of American domestic politics change, however, Congress may try to increase its influence – especially if the ratio of co-operation and conflict in Chinese–American relations should change in favour of conflict.

The OPEC countries Saudi Arabia, Iraq and Iran have remained the centre of conflict. A lot points to the fact that the USA and China will in the near future bump into each other even harder in the Middle East. Both countries are forced to risk a lot in order to secure their future energy supply.

China is actually not in the position nor willing to step into a direct military confrontation with the USA, and will also politically not have the say in the region. But through its strength as an economic partner, or more precisely as a reliable, long-term customer and investor it will be able to constantly strengthen its political weight. The international diplomacy that concerns itself with these issues will have to learn to view them from a new economic perspective. The political scope of action will be determined even more strongly than before by economic developments – a trend by the way, which countries such as Germany with a weak army and a still influential economy could use to their advantage.

Although Iraq is in the meantime lost for China, the next thrust of these developments is already taking shape in Iran. China attempts to replace the established economic powerhouse Japan, which covers 86 per cent of its oil consumption with imports from the Middle East, as Iran's most important partner in the oil and gas business.

An oil- and gas-pipeline could be laid from Iran via Central Asia to China – an option that is not available for supplies from any other of the four large oil producing countries in the Persian Gulf due to geographical reasons. Several long-term agreements have already been reached, and China's investments in Iran now total 100 billion US dollars. According to an agreement from October 2004, China Petroleum and Chemical Corporation (Sinopec) alone plans to import Iranian oil and gas worth 70 billion US dollars. Since the beginning of the third Iraq war the economic relations between China and Iran have become even closer. In 2004 Iran was the number one of the OPEC states, although the USA intensified its sanctions against the country and has described its nuclear weapons programme as 'intolerable'.⁷⁴ The Chinese at that moment acted calmly politically. Soon afterwards Norinco, China's largest trading and armaments group received the contract for the construction of Teheran's second underground railway line to the value of 836 million US dollars.⁷⁵ The state enterprise could offer a political price and thereby outdo Siemens amongst others. The Americans had imposed sanctions against Norinco in advance because of suspicions regarding the supply of nuclear technology.⁷⁶ In the autumn of 2004 the concealed confrontation between the USA and China intensified. 'We cannot permit that one of the supporters of international terrorism is developing nuclear weapons and delivering them to Europe, Central Asia and the near east' stressed John Bolton, the then US Undersecretary of State for weapon control and international relations in the State Department.⁷⁷

Colin Powell, the then Secretary of State added a little later: 'that's the limit. We will not allow Iran to become a nuclear power.'⁷⁸ The magazine *Newsweek* had reported in September that the US government was

preparing for a change in government in Iran, which was to be coerced through secret operations and if necessary with a force of arms.⁷⁹

China resisted the American advance with nothing less than the biggest energy contract in its history. The oil group Sinopec signed a preliminary agreement in the autumn of 2004 to the tune of 70 billion US dollars. China will buy 250 million tons of liquid gas over a period of 25 years and will develop the massive Yadavaran field. Additionally Iran has committed itself to selling China 150,000 barrels of oil a day, at the market price existing at that time, for the next 25 years. So far China had not received more than 13 per cent of its oil imports from Iran. The Chinese leadership wanted to close the deal as inconspicuously as possible. The Iranian oil minister Bijan Namdar Zanganeh however expressed himself decidedly:

‘For historical reasons Japan is our biggest importer of energy. But we now want to give preference to China.’⁸⁰ Whereupon Li Zhaoxing, China’s Minister of Foreign Affairs also took a clear position on the question, if the case of Iran, as the USA suggested, should be heard in front of the UN Security Council. ‘It would make this case more difficult and more complicated to solve it’.⁸¹

The deal is perfectly obvious: China protects Iran from the USA and in return gains guaranteed access to the mineral resources of the second most important OPEC state. Differently than in Iraq, China’s odds in Iran are decidedly better. The USA cannot afford to invade there; both from a military and political perspective. In the meanwhile China also comes into play politically: that the disarmament experts of the three most important European nations, Germany, France and England are to mediate and a way out is already been indicated. The closer the economic relationship with China becomes, the safer Iran feels and so it increases the possibility of the renunciation of its nuclear programme.⁸² Although the USA was manoeuvring, they took the pressure out of the conflict. ‘We do not have any plans for a change of regime’, said Colin Powell, the US Secretary of State in mid-November. ‘However we do not welcome this regime.’ But it has apparently not planned to invade Iran with the help of the 140,000 US soldiers stationed in neighbouring Iraq. He stressed that it was a matter for the Iranian people to decide over their future.⁸³ Ayatollah Ali Khomeini, the spiritual leader and head of Iran, accused the USA and Israel of waging an undeclared war on Islam. This war had overshadowed Ramadan, said the religious leader in his sermon at the end of the month of fasting in front of thousands of believers in Teheran.⁸⁴

The confrontation between the USA and China in the Middle East was of no importance for the Western media. In fact this conflict had

revealed itself for quite some time. The Chinese had already put Bill Clinton under pressure. In 1998, just before his trip to China he found himself forced to give in. On the 18th of May the US government allowed Western oil companies to invest in Iran.⁸⁵ An indirect apology from the Iranian President and the reformer Mohammed Khatami made Clinton's decision easier. But the economic pressures tipped the balance. China had begun to build a 2 billion US dollar pipeline through Iran and was negotiating with Iran's National Oil Company over the exploitation of the Iranian off-shore oil fields. Washington on the other hand still blocked the construction of an oil pipeline from the Caspian Sea through Iranian territory. In the previous year the Chinese had bought shares in Iraqi oil fields, which they lost in the third Iraq war. The newly gained economic position was also in this case immediately converted into political capital: 'we are very concerned about the fact that the Iraqi civilian population has to suffer in such a manner under the sanctions. I hope that the sanctions will soon be lifted,' glibed Qian Qichen, the former Foreign Minister and Vice Prime Minister at that time in the weeks before the summit. The USA and Iran have not maintained diplomatic contact for 27 years, whereas China and Iran have had diplomatic relations since 1971. The relations between Iran and the USA, which had existed openly since the fifties, became closer until the Islamic revolution in 1979, when the US-friendly but feudal Shah monarchy was toppled and replaced with a religious state.⁸⁶ From then on the USA was regarded as the mortal enemy. In November 1979 Khomeini's followers stormed the US embassy in Teheran. They took 50 Americans as hostages for over 400 days with the aim of forcing the extradition of the Shah, who was in the USA for medical treatment. In the course of the continuous eight-year war between Iran and Iraq, the first Gulf war, the USA became friendlier to the Baath regime in Baghdad. Eventually the Iraqi army received weapons, equipment and important military information. On several occasions it came to (military) engagements between the Iranian navy and the US navy, which had also attacked the Iranian drilling rigs. Only several days before Teheran consented to a UN-mediated armistice with Iraq, the US cruiser 'USS Vincennes' erroneously shot down an Iranian airliner. All 290 people on board were killed. The trade embargos imposed by the USA against Iran remained in force up to the devastating earthquake in the Iranian province of Kerman in 2003. Iran and the USA's history is therefore very strained. How this conflict will continue to develop, is difficult to predict. One thing at least is becoming clear – the more powerful the Chinese economy become, the blunter the threat of American economic sanctions will surely be, and the more expensive and more difficult military actions will prove themselves. China is

therefore in a favourable position. It can increasingly develop its co-operation with the states of the Middle East, whilst the USA can only make itself heard and gain respect through political pressure. Peter Scholl-Latour used the appropriate description with the title of a book in which he depicts the USA as a 'world power in quick sand'. China on the other hand is circling in the thermals of the hot desert.