

Courting the prize in Pakistan

India, China and the geopolitics of Iranian gas

While China's rapidly growing demand for energy imports is well known, less attention is paid to another rising Asian giant: India. India's energy needs are also soaring, and since many of its fossil fuel sources are identical to China's, some might say that competition and even conflict looms. How will they manage a vital future supplier – Iran – and a key potential transit country – Pakistan – and how might their interests intersect?

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SINCE THE FOUNDING of the modern Republic of India and People's Republic of China (PRC) both have been engaged in a long-running security dilemma fuelled by Cold War politics, regional alliances and territorial disputes. Even before we factor in potential disputes over energy, we can observe a slow-burning conflict of interests. Fearing 'strategic encirclement', India wishes to reduce Chinese influence over its neighbours (such as Pakistan) while China is dead-set against Indian aspirations of regional hegemony (Garver, 2001).

Meanwhile, Iran's major hydrocarbon reserves, its geographical location and its prickly relations with America make it a particularly interesting potential supplier. India's growing need for natural gas means it is looking to Iran – which brings it into something of a *ménage-a-trois* with its arch-rivals China and Pakistan. What are India and China's plans for courting the prize, and how do those plans relate to each other?

Rising China, shining India

It is necessary to understand a little about India and China's internal issues and how this affects energy demand. India's population continues to expand rapidly. By 2007 it stood at 1.13 billion compared to China's 1.32 billion: within a couple of decades it could well overtake China. But in terms of both total and per capita GDP, India is well behind its neighbour.

The IMF estimates India's growth in 2009 at just over 6%, more than twice the unimpressive 'Hindu rate of growth' prior to recent reforms. Such rapid change inevitably heightens the schisms within Indian society and India's rulers must assuage the anxieties of both the middle classes and the deprived rural population. Keeping a grip on such a difficult balancing act implies maintaining economic progress and thus energy security.

India's energy mix is more gas-based than China's: the amount of gas-fired electricity generation is rising by 7.5% per year. About 70% of India's increase in gas demand – which went up 38.7% between 1995 and 2000, and another 36.1% from 2000 to 2005 – is due to the power-generation sector (Vikas and Ellsworth, 2006). By 2025, the plan is for gas to take up 20% of primary consumption (Pandian, 2005).

However, India's gas reserves have only about 36 years to run, compared to China's 47. Now that India's gas demand has begun to outstrip its own production, it will have to find more sources – in 2004, it imported 2.6 billion cubic metres (Bcm) of Liquefied Natural Gas (LNG) from Qatar, and it will need more and more as growth continues (EIA, 2008).

There are some similarities with China's situation. IMF statistics show that ever since the turn of the century, the PRC has experienced double-digit growth. The governing Chinese Communist Party (CCP) cannot allow this stunning development to derail; such a disaster would not only dislodge the Party but could throw the country into disorder (Wang, 2005). The global slowdown was already beginning to affect employment in late 2008, however, and fears of unrest were growing.

So in order for growth to continue at all, the PRC's manufacturing-based economy also needs fuel, and lots of it. Gas use tripled from 1999 to 2007. In 2007 China was still producing enough gas for its needs, but in the likely event that consumption outstrips production – just as it may in India – it too will soon become a net importer. Moreover, to help reduce pollution the CCP intends to move from coal to gas for its power generation needs (Jiang, 2006).

The pipeline

At present, both India and China obtain high proportions of their imported fossil fuels from the Persian Gulf. Iran is the 'ace in the deck', counting for 11.2% of world oil and 15.7% of gas – this puts it just behind Russia in terms of the proportion

of world gas and oil in million tons of oil equivalent (Mtoe). India and Iran are historic partners, and Iran is the source of about 10% of India's oil, ranking third in 2004 behind Saudi Arabia and Kuwait. More importantly, now that India is moving towards natural gas in its energy mix, Iran is potentially India's most critical gas supplier too.

For several years there has been talk of an Iran-Pakistan-India (IPI) natural gas pipeline. Around 2,775 km long, its capacity would be 150 million cubic metres per day: the project is valued at over \$7 billion. But the first problem is price. Beyond India's actual demand for energy, the IPI is also about relative cost savings of natural gas over LNG. It remains to be seen whether a price acceptable for all parties can be decided; the wrangling has continued well into 2009.

The second problem is Pakistan. Due to the interminable debate over Kashmir and India's perennial suspicions of Pakistan as a harbour for Islamic extremists, the Indian government has publicly stated that it must be Iran's responsibility to ensure the safe delivery of gas to India rather than Islamabad's. This puts Iran in a sticky position, turning haggling over gas prices from a mere trade dispute into an international political issue too.

The third problem is capacity. In the long term there is a question mark as to whether Iran is even capable of supplying all the energy it promises. The combination of American sanctions and Iran's prohibition of foreign ownership has resulted in deterioration of its energy infrastructure. There is a real danger that Iran won't be able to meet demand as it increases.

And then there's the geopolitics. If India's relationship with Iran is well established, China's is even more so. Significantly, China is heavily involved in Iran's oil and gas development. In 2004, for example, several major gas deals were signed to the tune of \$100bn over a 30 year period, and China is also investing \$750m in Iran's Yadaravan gas field (Garver, 2006).

Were the IPI to go ahead, there is Pakistan to consider too. Whoever has the most influence over Pakistan if it becomes a key energy corridor commands an element of power over their strategic opponent. If China took the upper hand in Pakistan, it would have the option to make India's energy access more difficult, and vice versa.

It is telling that, despite Pakistan's dealings with Washington, the Sino-Pakistan relationship has arguably been the most stable of all Beijing's foreign contacts over the last 50 years. A strong Pakistan is useful for China in countering Indian regional hegemony, and historically, whenever the US has aided India, China has responded by building up Pakistan (Garver, 2001). Beyond China's political and military support, Sino-Pakistani economic relations have also been strong.

The advantage may thus pass to China, and indeed in 2008 there were reports that Beijing had already expressed an interest in the IPI project. Since Islamabad and Tehran are already agreed on the price of Pakistan's share of the gas coming through the pipeline, if New Delhi continues to drag its feet then Beijing could step in and take the Iranian gas for itself (Economic Times, 2008).

The port

In fact, China's energy policy regarding Iran and Pakistan is already beginning to impinge on India's interests. While India develops the Chahbahar port in Iran, 200 kilometres to the east Chinese transnational companies continue to sponsor a rival project at Gwadar in Pakistan.

Aiming to emulate Rotterdam, Dubai and China's Special Economic Zone (SEZ) at Shenzhen (Arthur D. Little, 2006), the former fishing town of Gwadar is intended to become



an internationally competitive port facility. The facility will be linked to Iran and Karachi via the Makran coastal road, for which the Asian Development Bank is contributing \$500m (Hassan, 2002).

The first phase of Gwadar's construction was sponsored mainly by China, which contributed an estimated \$200m, 80% of the \$248m costs (Fazl-e-Haider, 2007). Phase 2 construction costs alone are estimated at around \$600m, and China has already pledged \$200m (Garver, 2006).

Much of that Chinese investment is down to Gwadar's potential as an 'energy hub'. As a major regional container port and refining facility, Gwadar's final role as an 'energy hub' could be as the meeting point of no less than five oil and gas pipelines – including the fabled Turkmenistan-Afghanistan-Pakistan-India (TAP[1]) pipeline.

So, should China take over the Iran-Pakistan pipeline, it already has an advantage over India. Gwadar's geostrategic position is clearly useful for China – otherwise, why pay? It is in a good location to connect to China's disadvantaged western province of Xinjiang, for example, and could serve as a useful 'port of call' for the People's Liberation Army Navy too. Should Beijing need to protect oil supplies from the Gulf in the event of a confrontation with Washington, New Delhi or Tokyo, it might even act as a temporary military base (Niazi, 2005).

Thus India has reasons to desire the downfall of the Gwadar project: if Gwadar failed it would boost Chabahar; it would degrade China's potential to siphon off Iranian and Gulf energy; and it would deny the Chinese a naval outpost to cover the Straits of Hormuz. In this sense, Gwadar could become a focal point of the destructive competition for energy and transit options.

China is downplaying the significance of Gwadar for India. Chinese analysts note that if Beijing wanted to control the port it could, but it has allowed the independent Singapore Port Authority to control it so as not to ignite tensions with India.

On the other hand, in economic terms, India could benefit from Gwadar's refinery capacities and as a potential terminal for the TAP(I) and a reference point for the IPI. Buying energy via Gwadar would bind India into a complementary commercial relationship with Pakistan and China that would have benefits for all. And China's construction of a conducive environment for Pakistan as an energy hub could even do India a favour by encouraging growth and stability in Pakistan, thus reducing the risk of an explosion over Kashmir.

Yet there has been little indication that New Delhi is about to sign a deal on the IPI. With its sanctions regime against Iran, Washington remains against the IPI pipeline and in 2008 the Congress government signed a controversial nuclear deal with the Bush administration. This deal played into the hands of leftist and Hindu nationalist political parties, and in India, such things can be vote-winners.

When it comes to courting the prize of Iranian gas, and striking a deal to transport it, China holds the advantage over India. The truth will ultimately be told in some decades time when domestic reserves of natural gas begin to dwindle. Only then might New Delhi regret missing the opportunity to share the prize with China and Pakistan – and look upon them as rivals even more.

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