

Liam Fox speech at Chatham House on defence & energy security

In a speech at Chatham House on the challenge of defence and energy security, Shadow Defence Secretary, Dr Liam Fox, will say:

Check against delivery

“What is the point of defence? It seems a relevant enough question in itself. It is given added importance when Whitehall departments are in constant competition for resources to feed our seemingly insatiable appetite for wealth consumption. This year we will spend only 2.2% of our GDP on defence – the lowest proportion of our national wealth contributed to security since 1930. Is it enough? Is it just right? Or is it even too much? Moreover, what is it being spent for?

The answer to the first of these questions appears, on the surface, relatively simple: safeguarding our borders; defending our homeland; and protecting our strategic national interests overseas.

But in this post-Cold War era of global free trade, what are our national strategic interests. What is the extent and nature of the threats we face?

Globalisation has brought shared risks. We live in a sophisticated, inter-dependent global economy where downturn, disaster or depression ricochets around the world, affecting us all. Equilibrium had been maintained in recent years by the voracious appetite of the American consumer driving the world economy while Europe and Japan struggled. Now growth gains its momentum from China, India and East Asia. Last year, incidentally, was the first year since 1842 that the majority of the

world's wealth was created in the East rather than the West.

Such interdependency brings its own problems though. We are all competing for the same natural resources to feed the economic system. The potential for terrorists or even nation states to interrupt this supply to cause widespread – rather than just local – disruption increases enormously. And this complex and sophisticated economy with its 24-hour trading and instant communication has developed independently from – perhaps despite – our political and security arrangements. As a result the 21st Century world economy exists in a defence framework designed for the Cold War and political structures that resulted from the post-World War Two settlement.

In the years ahead energy security, economic security and national security will be inextricably linked. If we want to ensure that we can keep the lights on in Britain then we need to develop a comprehensive energy strategy. It is simply a matter of risk management. Such a strategy will need to have three components: diversity in the type of fuels we use; diversity in the geographical sources of those fuels and the security structures that will guarantee the safe transport of these fuels.

THE STRAIN ON NATURAL RESOURCES

Any security strategy for energy will have to be conducted against a difficult international backdrop and we will have to balance complex, competing global economic, environmental and political interests.

As the world economy grows and living standards rise across the

developed world, global demand for energy will continue to increase.

Even minimal interruption to energy supply can cause havoc. We all remember the power cuts which crippled California in 2000 or parts of England in October 2002 after storms. If you were to stop and think for a second, I am sure you would realise how the lack of electric power would adversely impact on our own daily life – from the morning commute to the evening soap opera. It is a startling fact that in the UK we have only eleven days power supply at any one time. And we will be obtaining that energy in future in a world where there is fast growing demand.

In 2004, global oil production exceeded 80 million barrels of oil a day for the first time.

Between 2003-4, OPEC increased oil production by 7.7%, Russia by 8.9% but China by only 2.9% yet China's consumption grew by 16%.

Oil demand is predicted to reach 120 million barrels a day by 2025. China's demand alone will triple by that time.

Meeting this demand will not be easy. There is little spare refining capacity outside of Saudi Arabia to deal with spikes in demand.

Most of the non-OPEC reserves are in either West Africa (Gulf of Guinea) or in the difficult but potentially huge tar reserves in Alberta. Similar difficulties apply to other hard-to-reach resources such as shale or coal-bed methane and global competition for the investment needed to develop these new resources is intense.

To see this picture in context let me take a closer look at the world's fastest growing economy- China.

Today, China accounts for 12% of the world's energy consumption, up

from 9% only a decade ago. That is second only to the United States at 24%. The director of energy economics and development strategy at China's national development and reform commission has estimated that by 2010, oil will account for around 52% of China's energy needs, up from 29% in 2000

And that oil will increasingly need to be imported. In 1993 only 6% of China's oil was imported. Today that figure stands at 60%.

When we consider the impact of other fast growing economies- India, for example, or the countries around the Pacific Rim - we can see the scale of what we are dealing with. All of this is complicated by the fact that much of this fuel supply comes from politically volatile parts of the world, notably the Middle East. Again, China is an interesting example.

Today, 58% of China's oil imports come from the Middle East. The IEA expects Chinese oil imports from the Middle East to rise to at least 70% by 2015. The China National petroleum and chemical Corporation (Sinopec) has scored big successes in both Iran and Saudi Arabia: a \$100 billion contract with Iran to buy 10 million tonnes of liquefied natural gas per year over 25 years, and a 50% stake in the Yadaravan oilfield. Thus, the future of the world's fastest growing economy, the new engine of global growth, is hugely dependent on the stability of the Middle East.

HOW DEPENDENT ARE WE?

What about the position here in the UK? Clearly energy security is no longer a matter solely of national sovereignty and indigenous production. The time when we could rely on the fuel sources under the ground in this country and around our shores are long gone. We now import half the coal we use. Estimates vary about the level of British coal reserves

potentially obtainable but current economics make an increase in mining unlikely in the short term.

And it isn't just coal. The fabled 'dash for gas' has come to a halt. In 2006, we will become net importers of gas for the first time since 1997. By 2010, we are likely to have become net importers of oil. Unlike, say, Iceland we do not have inexhaustible reserves of geothermal power. Nor in our crowded isle do we have Australia's HEP potential in the Snowy Mountains that powers Sydney. Renewables have a crucial role, as David Cameron has stressed, and we need significant investment in this field.

Our dependence on external sources of electricity has hit hitherto unknown levels. Indeed, according to the Government, by 2020 we may be reliant on overseas resources for 80% of our energy needs. As the Institute for Civil Engineers has pointed out: "This country has been self-sufficient in electricity generation for the past 100 years. This is about to change dramatically. The (domestic) generation shortfall (80 per cent of current capacity) will be taken up by gas, 90 per cent of which will be delivered to this country through a very small number of pipelines".

There is also a problem of storage and transmission. We have a much lower level of strategic gas storage in the UK than in France and Germany. Whilst our gas storage capacity will have doubled by 2010, we will still lag behind many of our European neighbours, which makes us all the more vulnerable to volatility in gas deliveries.

We are relying for gas on a pipeline from Belgium. As domestic gas production falls, what if our neighbours find they don't have the surplus gas to export to us? Who is to say Russia, the obvious alternative, will

remain stable?

THE CHANGING NATURE OF THE THREAT

As the international picture grows more complex, so our security policy needs to become more agile and flexible. Our political and military structures date from another -Cold War-era, ill-suited to a world where we need those structures to reflect the new threats. Inter-state diplomacy through the IEA, EU or G8 is insufficient when the threat is no longer state-to-state but asymmetric attacks by non-state actors. These will disrupt the world economy not just by the material consequences of an attack but equally by the atmosphere such an attack would create around the world.

Whilst the US has only limited strategic interests in the global gas market, it does have massive strategic interests in oil given it consumes a quarter of the world's production. Many of the United States' foreign policy concerns at the moment arise from developments in the oil trade. This is why President Bush is trying to wean America off its addiction to oil. Embracing biomass is as much a matter of strategic geopolitics for President Bush as it is environmentalism.

The problems are compounded by the lack of political stability in many oil-producing areas which inhibits necessary overseas investment, and this is aggravated by those states that for political reasons refuse overseas investment. Both lead to eventual compromises in supply.

But the real problem is not so much scarcity of resources as concentration of easy-to-reach supplies in politically-difficult areas, along with the additional problem of transporting these supplies through areas that are

equally difficult politically. The focus is not merely on the country with the hole in the ground, but also the transit countries through which the gas flows, and the sea lanes through which the oil must be transported. Instability and interruption of supply in any one transit country along these latter-day “silk routes” is as damaging as it would be at source.

The distribution of global energy supplies means we are particularly vulnerable to the ‘choke points’ in transport routes around the globe. These are far more numerous than the days when we patrolled the Straits of Hormuz. They are scattered from the Panama Canal to the Bab el Mandeb Strait at the entrance to the Red Sea to the island-scattered seas of South East Asia. And that is before we even consider the growing problem of piracy, especially off the Horn of Africa.

No oil installation is attack-proof. The impact of a limited attack on a single site may be more a matter of the atmosphere created than the material damage – but it will damage confidence, even if the impact on supplies is tiny, as well as pushing up oil prices yet further.

Osama bin Laden has not described infrastructure such as oil refineries as the “hinges” of the world economy for nothing.

But as with gas, energy security is not just a matter of the vulnerability of producer countries but also the vulnerability of transportation routes – in the case of oil, either by sea or by pipe. It would be no surprise if al-Qaeda were to be planning to blow up a super tanker in the Straits of Malacca. It would cause economic panic, regional tension, an environmental catastrophe, and an increase in the price of fuel impossible to calculate.

ENERGY AS A WEAPON-THE RISE OF RESOURCE NATIONALISM

But there is another problem for us to consider. ‘Resource nationalism’ has seen countries attempt to use their oil and gas to extract technological concessions from other countries trying to buy that oil and gas. In some instances, such as China, this is accompanied by an unwillingness to surrender natural resources to ‘foreigners’.

These areas are not noted for their political stability or natural warmth towards the West. Gas will come from Russia, the Caspian Basin and the Middle East – all volatile and all inclined to use their natural resources as bargaining chips in international diplomacy, as Venezuela is doing in its ‘cold feud’ with the US.

In Venezuela, President Chavez’s closure of the ‘apertura petrolera’ – which had left Venezuelans poorer than they were thirty years ago, despite all the oil dollars – is part of a strategy to oppose what he sees as US imperialism in South America. Giving preference to other South American states as oil customers is one way for Venezuela to create ‘solidarity’ within the continent.

Evo Morales, newly-elected President of Bolivia, has just nationalised his country’s gas industry. The sight of Presidents Morales and Chavez with Fidel Castro in Cuba should give pause for thought. And with their choice of Ken Livingstone as their British best friend, the prosecution rests.

“THE RUSSIAN THREAT”

We have become well-versed in dealing with sometimes unstable oil-producing nations through cautious diplomacy and the use of OPEC. As a

growing reliance on gas brings new supplier countries to the fore, we will face a differing set of challenges – challenges we may have to face without guaranteed American involvement, since the US focus is currently more on oil than gas. This may change with the development of the Shtokman gasfield in the Barents Sea, but that is some way off fruition.

The concentration of gas supplies in the territories of the former Soviet Union is an issue related not merely to the business world, but to geopolitics and international relations in general. A quarter of Russia's GDP, a third of its industrial output and half of its federal revenues are dependent upon their energy resources.

Producer and transit countries may not always be pulling in the same direction, as the tensions between Ukraine and Russia illustrate. When Russia reduced supplies to the Ukraine as part of a bilateral dispute, supplies to Europe also fell by a third. Of course it works both ways: Other countries allegedly siphon off Russia's gas, receiving preferential deals yet still not paying their bills – if ever. Moldova's main power station doesn't pay them at all. In 2005, the Ukraine was paying \$50 per 1,000 cubic metres compared to the EU's \$240. The price of stable, cheap supplies appears to be subordination to Russia – as the experience of Belarus demonstrates.

Territorial disputes will also continue lurking beneath the surface. The Crimea, for example, was gifted by Khrushchev in 1954 from Russia to the Ukraine – a semantic gesture in a totalitarian state, but a live one between two nations of an occasional nationalist disposition.

We will need to keep an eye on the Russian domestic energy market, out of which some worrying signals are emerging. Back in April, Gazprom's chief executive Alexi Miller warned the EU against any attempt to interfere with its possible purchase of Centrica. "Attempts to limit Gazprom's activities," he said "in the European market and to politicise questions of gas supply, which are in fact entirely within the economic sphere, will not produce good results". He did not specify what these 'not good results' might be – political, military or economic is unclear. But President Putin's address to the National Assembly cannot be ignored. It contained substantial passages detailing his plans to enhance Russia's military capabilities. And Russia's military security and energy security are as interlinked as anyone else's.

State-owned Gazprom and the wider clique of Russian mineral oligarchs are inevitably influenced by – and influence in turn – the wider strategic purpose of the Putin administration. These state-run corporations have ambitions as much political as economic – consider the fate of Yukos. Much of the Russian energy sector is dominated by the so-called *siloviki*, former intelligence officers with a similar background to that of President Putin himself. Given the unpredictable future political direction of Russia after President Putin (however far away that is), and with an uncertain role for oligarchs themselves enriched by the global energy market, Gazprom's business strategy must remain a matter of concern to foreign governments. It might be considered an irony that "energy security" is the key theme of this year's Russian presidency of the G8. It must be seen as an unmissable opportunity.

CHINA'S RAW MATERIALS EMPIRE

And what of China?

Wenran Jiang of Washington's Jamestown Institute has recently written of the popular Chinese online novel *The Battle in Protecting Key Oil Routes* which looks forward to a decisive naval engagement in the Straits of Malacca, linking the Indian Ocean and South China Sea, where a Chinese navy defeats a US fleet.

Given that a quarter of global oil transits these Straits, their strategic importance cannot be overstated. Almost as important are the Lombok and Makassar Straits in Indonesia.

The failure of the China National Offshore Oil Corporation's bid for the US UNOCAL petroleum company has forced China to look elsewhere to satisfy its own need for energy security, and encouraged those who believe China needs to build a 'blue water' navy to protect the sea routes to the Middle East. The fact a potential land pipeline route also exists partly explains Chinese (admittedly somewhat cool) "tolerance" of current Iranian policy. It would be no real surprise if in the medium-term future we saw Chinese aircraft carriers patrolling the Straits of Hormuz protecting their oil routes.

China is slowly bringing about a "string of pearls" strategy for naval bases from the Middle East to the South China Sea. The list includes a new base under construction at the Pakistani port of Gwadar, where Beijing already has an electronic eavesdropping post to monitor Persian Gulf traffic. There is also a proposed pipeline through Islamabad, and over the Karakoram Highway to Kashgar in Xinjiang province, which would transport the fuel to the PRC itself. Other "pearls" include a container port facility at Chittagong, Bangladesh; a naval base under construction in Burma; and intelligence gathering facilities on islands in the Bay of Bengal and near the Strait of Malacca. The Chinese have been

viewing the modernisation by India of military facilities on the Andaman and Nicobar Islands with particular suspicion.

I welcome, therefore, the tri-lateral monitoring agreement between Singapore, Malaysia and Indonesia that will help secure the Straits of Malacca. It is a welcome first step.

As I told the Heritage Foundation last year: “How China will evolve, and how it will impact on the rest of the world, is dependent on a number of complex interactions ... There are different pathways that China could take. Either the great economic miracle could continue, in which case China could become a major economic power with gradually developing political institutions based on free market philosophy, the rule of law and respect for human rights or it could remain economically successful while retaining its internal repression and use its economic might to finance expansionist policies with a well-resourced military”. Of course, China could fail economically with who knows what consequences.

Deng Xiaoping, back in 1985, enunciated China’s future goals as being ‘peace and development’, and much of China’s foreign policy can be interpreted as securing China’s economic growth. China sees economic growth as the access-point to geopolitical influence. And Chinese trade – and investment – is economically important to us.

There are huge opportunities, both political and economic, in a developing China. There is a danger that if we identify China as a potential future enemy, it inevitably will start to act like one now.

“ALL POLITICS IS GEOLOGY”

Oil and gas are just two of the natural resources which act as the drivers

of foreign policy. Niche mineral resources can gain sudden prominence – just as gallium did with the explosion in mobile phone usage. This had a significant impact on the economy of Rwanda – the main source of gallium – and played a key role in that country’s unstable recent history. With the unpredictable nature of future technological developments, future mineral needs are equally unpredictable – but the location of most of the world’s tungsten in China and North Korea is surely one that cannot be overlooked.

With 90 percent of the world's cobalt, 64 percent of its manganese, 50 percent of gold, 40 percent of platinum, 30 percent of uranium, and 20 percent of the total petroleum currently traded, Africa is a treasure trove of strategic raw materials, much coveted by Chinese trade missions. Forty percent of the world's potential hydroelectric power lies unharnessed in sub-Saharan Africa. So whilst Beijing’s decision to prop up the Mugabe regime in Zimbabwe may seem odd, but it seems less so when set against Zimbabwe’s vast mineral and precious metal deposits which China covets.

Chinese support for the Sudanese regime perpetrating the atrocities of Darfur must also be seen through the prism of the China National Petroleum Company’s massive investments in the oil industry there. Is no excuse, however, for China turning a blind eye to human rights violations.

We might be tempted to think that all politics is geology now. Yet none of this is really new. Patterns in the expansion of Phoenician territorial control in the Ancient World were linked to the main trading routes. The work of the French historian Fernand Braudel brilliantly explored the interlinkage of economics, geography and social development in the

Mediterranean. The thirst for empire from the Spanish onwards was often driven by economic pursuits, not least for gold.

HOW DO WE RESPOND?

So concern for natural resources is hardly a new phenomenon. But the very fact of Marshall McLuhan's ever more complex "global village" makes ensuring our energy security ever more difficult. We have to balance our security through both effective military structures to underpin our diplomacy, for without them, diplomacy is like an empty gesture. Equally, our security will require a balanced and varied portfolio of energy sources, including renewables. In that light, the case made by David Cameron for greater investment in renewable energy can be seen in its wider context. Greater availability of renewables is not simply an environmentally desirable end, but by diminishing dependence on external supply, increases economic and thereby national security.

It is this 'variety' which will enable us to survive the likely shocks to the global economy which will inevitably occur. But variety of geographical source alone will not suffice.

An indivisible energy security and national security policy will inevitably have consequences for the necessary shape and capabilities of the armed forces required to pursue those interests. Over and above that, it will have consequences for the intellectual approach the Ministry of Defence must adopt towards global affairs more generally. This requires clearer political leadership, as well as greater analysis of our security requirements.

As Paul Cornish, the head of the security studies here at Chatham House, stated so succinctly in his inaugural speech, it is sometimes the case that

too much is expected of our armed forces and the Ministry of Defence. It is not that our military don't have the capability to deliver but it is that they are being placed in an invidious position – that of becoming a political end in themselves rather than a tool of political leadership and policy execution. This has been especially clear in Iraq where military success has become the main objective rather than merely a pre-cursor to such political imperatives as nation-building, stability, democracy and personal security. Military success cannot be a replacement, subsidiary goal merely because the political challenges appear too great.

Politicians need to provide a much clearer framework within which national security interests can be served. In other words, we need a foreign policy out of which a credible defence policy – rather than merely spending plans – can flow.

Interruptions to gas supply have far less impact on the US than on us, so we cannot necessarily expect anything more than good wishes from Washington. Hanging on to American coat-tails in the Caspian Basin – a politically fickle region – is an inadequate strategy, since that involvement is part of the War on Terror rather than the war on energy insecurity. Russian hostility to that American involvement merely complicates matters.

We must remember that what impacts on Baku impacts also on Darlington. We need to consider how to balance our competing national interests in respect of terrorism and energy security to assess how we relate to President Sakalashvili in Georgia, towards how we bolster Azeri internal security, how we view arm sales to Kazakhstan, or promote a resolution of the underlying conflicts in Nagorno-Karabakh and

Chechnya.

EUROPEAN COOPERATION

As a Euro sceptic, you may think it strange for me to advocate a European security solution, but I believe that the European nations – not, I stress, the EU as an institution – need to come together as a consortium of energy consumers to bring their collective weight to bear. Only that way will we mitigate any risk of ‘divide and rule’ policies on the part of Russia and other suppliers from having an impact on gas supply.

What we cannot do is leave it solely to the EU as an institution. A report for the EU on energy security drawn up in 2004 paints a worrying picture:

“To the extent that member states find it necessary to forge national security of supply policies at the level of national foreign policy-making, this strategy to deal with supply concerns will not only interfere with EU energy policies but could have negative effects on the development of EU foreign and security policies”.

We cannot allow our own national energy security to be held to ransom by the dreams of Brussels for creating foreign and security policy integration. Yet strangely to some, it is the usually integrationist nations such as Germany who are acting independently at the moment. Gerhard Schroeder invested much time and effort as Chancellor in improving relations between Germany and Russia, and since Angela Merkel’s victory, he has played a crucial role in the Russia-Germany Baltic pipeline project. This is a project which has caused jitters in Warsaw and the Baltics. Their concern is perhaps understandable. It was less than 20

years ago that the Russians turned off the oil in a bid to forestall Baltic independence.

Yet the real threat is not some 'Bond villain'-like tyrant holding the world to ransom as much as sudden asymmetric terrorist attacks on major processing plants or transit pipelines. Supporting, training, and building military capacity in transit countries is an important strategic objective given the danger of terrorist strikes on transit facilities. This is a role for which NATO is uniquely suited, and which it is already tentatively engaged in with the Partnership for Peace programme. But despite much recent talk, NATO membership for Caucasus nations is still some way off. Yet NATO must accelerate its efforts, and have our energy security uppermost in its strategic thinking.

The NATO-Russia dialogue especially must not be an exercise in routine summitry, but rather a practical initiative to improve mutual confidence and ensure the continuation of gas supplies. Indeed, NATO exists to address the security concerns of its member states and guarantee peace and stability – and energy supplies are one of the most crucial of those security concerns.

It is worth noting that the Polish government has recently called for an 'energy pact' similar to the mutual defence clause underpinning NATO, whereby all EU countries pledge to come to each other's aid in the event of an energy crisis. It is an idea that deserves serious exploration. Hungary is 80% dependent on Russia for its oil and gas. How would we respond in the event that a dispute between the two countries resulted in Russia turning off the tap?

Key contributors to recent major operations have tended to be from allies that are not part of NATO. In either Iraq or Afghanistan or both, contributions have been made from nations such as Australia, New Zealand, South Korea, and Japan. Such countries have also contributed to NATO-led and other Coalition operations. For example, New Zealand has contributed forces to NATO-led operations in the Balkans and is currently contributing forces to ISAF in Afghanistan.

There is currently momentum within the Alliance for this and moves towards greater involvement by such countries have already begun. Most recently, in February, the New Zealand Defence Minister, Phil Goff, signed an agreement on the exchange of classified information with the NATO Secretary General. Furthermore, the first address by a Japanese Foreign Minister has just been made to the North Atlantic Council.

It is therefore important that NATO develops associations with nations and regions that can contribute to countering the key threats to our energy security. Therefore, NATO members and interested parties should be encouraged to form such associations, especially with the Pacific region. New structures will be required to counter new threats to our mutual interests. The structure and function of NATO itself needs to be assessed. It is big picture politics and I want the Conservative Party to be at its cutting edge.

As long as we perpetuate a situation where we are dependent on producer and transit countries, but not vice-versa, we will have an unacceptable asymmetry. And it should not be forgotten that Russia needs reliable consumers as much as we need a reliable supplier. As much as we need to keep an eye on the activities of the oligarchs and fuel giants, we should

also remember that the likes of Gazprom are thirsty for capital to replace their ageing Communist-era infrastructure.

Any ‘dependency’ relationship needs to be transformed into an ‘inter-dependency’ relationship. This means building better trade links, more effective investment overseas, improving educational and cultural links, and most importantly, improving connections with their respective militaries.

The UK’s Ministry of Defence has an established reputation in the military sphere, and I believe it would be a positive development to consider establishing an Energy Security Directorate within the Government. This could serve not only UK strategy, but also work with producer and transit countries to improve security and mechanisms for co-operation in case of challenges to supply.

The British Council also has a uniquely high reputation around the world, and could play a fundamental role in improving the educational and cultural links I spoke of. Our diplomatic footprint must also reflect the new global reality. Our embassies in the Caspian are more important than ever, and cannot merely be just a handful of people in a rented office.

Our mission in the regions of the world needs to be both economic and grounded in diplomacy, aimed at building security capacity.

When Churchill switched the navy from running on coal to running on oil, it meant we no longer depended on the Welsh pits but on the Persian oil fields. At that point, energy security became national security. Churchill said that ‘safety and certainty in oil lie in variety and variety

alone'. It was true then and true now.

We need to ensure that a variety of energy sources are available for our economy, be they coal or gas or nuclear or renewables. We need to ensure that they are drawn from different geographical regions to minimise the risk of disrupted production.

But our whole approach must be underpinned by a security margin of resilience which only updated global military structures can provide. The gauntlet has been thrown down to us. The question is whether we can, or will, rise to the challenge.”