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China's Oil Offensive Strikes: Horn of Africa and Beyond

By Andrew McGregor

In its efforts to expel an Islamist government and capture a handful of inactive al-Qaeda suspects in Somalia, the United States has risked its political reputation in the region through a series of unpopular measures. These include backing an unsuccessful attempt by warlords to take over the country, several ineffective air raids, and finally, the financing of an unpopular Ethiopian military intervention. As African Union peacekeepers struggle to restore stability in the capital of Mogadishu, China has stepped in to sign the first oil exploration deal negotiated by Somalia's new government. The agreement is the first of its kind since the overthrow of the Siad Barre regime in 1991 began a long period of political chaos in the strategically important nation.

China's four major oil corporations have unlimited government support, allowing them to edge out the smaller Western oil companies that traditionally take on high-risk exploration projects like Somalia. Latecomers to the global oil game, the Chinese companies and their exploration offshoots have focused on oil-bearing regions neglected by major Western operators because of political turmoil, insecurity, sanctions or embargoes. China once hoped to supply the bulk of its energy needs from deposits in its western province of Xinjiang, but disappointing reserve estimates and an exploding economy have given urgency to China's drive to secure its energy future. Twenty-five percent of China's crude oil imports now come from African sources.

The Somalia deal is part of a decades-long Chinese campaign to engage Africa through investment, development aid, "soft loans," arms sales and technology transfers. The European Union recently warned China that it would not participate in any debt-relief projects involving China's generous "soft-loans" in Africa (Reuters, July 30).

Global demand for oil is expected to rise over 50 percent in the next two decades even as prices rise and reserves decline. To meet this demand, China and other Asian countries offer massive infrastructure developments in exchange for oil rights. President Hu Jintao and other Chinese leaders are regular visitors to African capitals and Chinese direct investment in Africa totaled $50 billion last year.

Oil in Somalia?

Last month a deal was reached between Somali President Abdullahi Yusuf Ahmad,
the China National Offshore Oil Corporation (CNOOC) and China International Oil and Gas (CIOG) to begin oil exploration in the Mudug region of the semi-autonomous state of Puntland (northeast Somalia) (*Financial Times*, July 17). Somalia's Transitional Federal Government (TFG), which has yet to secure its rule, is to receive 51 percent of the potential revenues under the deal.

Somali President Abdullahi Yusuf (a native of Puntland) appears to have negotiated the deal in concert with Puntland officials but without the knowledge of the Prime Minister, Ali Muhammad Gedi, who is still working on legislation governing the oil industry and production-sharing agreements. Gedi insists that "in order to protect the wealth of the country and the interests of the Somali people, we cannot operate without a regulatory body, without rules and regulations" (*Financial Times*, July 17). The agreement with China may become an important test of the authority of the transitional government. China has effectively preempted the return of Western oil interests to Somalia, though it is unclear how the Chinese project may be affected by the passage of a new national oil bill. Somali negotiators assured the Chinese firms that new legislation would have no impact on exploration work due to begin in September (Shabelle Media Network, July 17).

Though Somalia has no proven reserves of oil, Range Resources, a small Australian oil company already active in Puntland, suggests that the area might yield 5 to 10 billion barrels (Shabelle Media Network, July 14). Somalia is also estimated to have 200 billion cubic feet of untapped natural gas reserves. Western petroleum corporations, however, conducted extensive exploration of potential oil-bearing sites in Somalia in the 1980s and found nothing worth developing.

Public unrest is already on the rise in Puntland as the local government grows increasingly authoritarian and the national treasury has mysteriously dried up. Discontent has accelerated as leaders of the one-party regime continue to sign resource development deals with Western and Arab companies without any form of public consultation. The new deal with China has the potential to ignite political unrest in one of the few areas of Somalia to have avoided the worst of the nation's brutal political nightmare.

China's Strategy in Africa

Last November, Beijing hosted an important summit meeting between Chinese leaders and representatives of 48 African countries. The African delegates gave unanimous support to a declaration endorsing a one-China policy and "China's peaceful reunification" [1]. China in turn announced a $5 billion African development fund (administered by China's Eximbank), with a promise of $15 billion more in aid and debt forgiveness to come. In exchange for secure energy supplies, China is also offering barrier-free access to Chinese markets, something Africans have been unable to obtain from the United States or the EU.

While China has had success in securing energy supplies in Africa, its oil offensive is by no means flawless. Chinese corporations working abroad provide little employment for local people and are remarkably tolerant of corruption and human rights abuses. Chinese overseas operations are also notorious for their disregard of environmental considerations. The latter is perhaps unsurprising, considering the environmental devastation afflicting China's own industrial centers. Yet, the combination of all these factors tends to create unrest in nations where Chinese operations are seen as benefiting members of the ruling elite and few others. What is also notable is that of the five African countries where China is involved in major resource operations, only one, Angola, is not dealing with a major insurgency.

Sudan

China continues to expand its operations in the Sudan, its most successful foreign energy project to date. Oil from southern Sudan currently supplies 10 percent of China's imported energy needs. Chinese and Malaysian companies operating as a joint venture (with a minority Sudanese share) stepped up to take over the exploitation of Sudan's vast oil reserves after international pressure forced out the Canadian Talisman Corporation. The China National Petroleum Corporation (CNPC) recently announced the acquisition of a 40 percent share in a major exploration site off the Sudanese Red Sea coast. A 1997 embargo prevents U.S. companies from operating in the Sudan.

The Sudanese/Swiss ABCO Corporation claims that preliminary drilling in Darfur revealed "abundant" reserves of oil. These reserves have yet to be confirmed, but it appears that the rights may have already passed into Chinese hands (AlertNet, June 15, 2005; *Guardian*, June 10, 2005).

Ethiopia

China and Malaysia, partners in the Sudan, are trying to replicate their Sudanese success in the Ogaden region of Ethiopia. As a demonstration of goodwill—and to increase the incentives for cooperation—China and Ethiopia signed a debt relief agreement in May worth $18.5 million (Xinhua, May 30). In addition, a new convention center for the African Union headquarters in Addis Ababa is being built with substantial Chinese assistance.

Following its usual practice, China imported its own labor to work in the Ogaden projects in preference to hiring local workers. Asian exploration companies tend to arrive in the region with large military escorts after negotiating contracts with the Tigrean-based government in Addis Ababa. The ethnic-Somali inhabitants of the Ogaden region have little input, making the operations a target of the rebel Ogaden National Liberation Front (ONLF). A commando unit of the ONLF attacked a well-guarded Chinese oil exploration facility in northern Ogaden on April 24, killing 65 Ethiopian troops and nine Chinese workers. A further seven Chinese workers were abducted "for their own safety" and released a week later (ONLF communiqué, April 24)

Niger

In Niger the CNPC (already active in two other concessions) appears to be in the lead for the sole rights to the promising Agadem concession, to be awarded sometime this month. With financial support from the Chinese government, CNPC is offering to build a refinery and a pipeline in exchange for the rights, a commitment even Western oil giants like Exxon have shied away from. A Tuareg-based rebel movement in the resource rich north has declared Chinese oil and uranium operations "unwelcome" while accusing China of supplying the Niger army with weapons to pacify the region. Rebels attacked an armed supply convoy heading to a CNPC exploration camp in July, killing four soldiers (Reuters, July 31).

NIGERIA

Last year, the CNOOC moved into territory previously dominated by major Western oil companies in the Niger Delta, paying $2.7 billion for a 45 percent share in an offshore oilfield expected to go into production in 2008 (Reuters, April 26, 2006). China is building $4 billion worth of oil facilities and other infrastructure in return for access to other promising Nigerian oil-fields, including the untapped inland Chad basin (BBC, April 26, 2006).

With a growing insurgency in the oil-rich Niger Delta threatening Nigeria's oil industry, China has stepped in to supply weapons, patrol boats and other military equipment. Beijing does not share Washington's reluctance to supply such hardware to a Nigerian military accused of corruption and human rights violations (*Financial Times*, February 27). The insurgents claim that Chinese, Dutch and U.S. resource companies fail to hire local labor and are devastating the local economy and environment through unchecked pollution. The world's eight largest oil exporter, Nigeria is also a major market for Chinese exports.

ANGOLA

Beijing has been wooing oil-rich Angola through promises of aid and development. Its promise of $2 billion in soft loans brought a guarantee of uninterrupted oil supplies to China and offshore exploration rights for CNPC while enabling Angola to avoid Western pressure to restructure a corrupt and inefficient economy.

COMPETITION WITH THE UNITED STATES

As China intensifies its economic engagement with Africa, the United States has been steadily increasing its military presence in Africa, supplying arms, training troops and opening new bases for U.S. personnel. Efforts such as the Trans-Saharan Counterterrorism Initiative have brought U.S. forces into many countries for the first time as part of the global effort against al-Qaeda. The creation last February of AFRICOM, a new U.S. regional combatant command for Africa, reflects Washington's new interest in the area. Despite the anti-terrorism rhetoric, it appears that the main function of AFRICOM will be to secure U.S. energy supplies in a region that is expected to provide a growing share of the United States' future energy needs.

Ironically, U.S. arms and military training provided under the guise of "counter-terrorism assistance" may ultimately provide Chinese oil interests with the security they need to carry out operations in high-risk areas. An Ethiopian army financed and equipped by the United States for use against "Al-Qaeda terrorists in Somalia" is now being used to protect Chinese oil exploration efforts in the Ogaden region through military operations against ONLF rebels and punitive attacks on ethnic-Somali civilians.

CONCLUSION

So far, a visible disinterest in tying resource development contracts to social or economic reforms has aided China in securing its energy future in Africa. To be fair, this pattern of tolerance for corruption in regimes with desirable natural resources was set long ago by Western corporations and governments. China still employs the rhetoric of anti-colonialism in its relations with Africa, but many Africans are beginning to see China as an exploitive major power supporting corrupt regimes in the same manner as the former Western imperial powers. While China is taking some small steps to correct this impression, problems will persist unless Africans see immediate benefits from the Chinese presence, particularly in the field of employment. China's success in presenting itself to the Third World as "the largest developing country" will eventually have limited currency if its business operations become indistinguishable from Western corporations. In the meantime, China's rivalry with the West for control of Africa's oil is certain to intensify.

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NOTES

1. See the full text of the Declaration of the Beijing Summit Of the Forum on China-Africa Cooperation, available online at: http://english.focacsummit.org/2006-11/16/content_6586.htm.

Arms, Energy and Commerce in Sino-Russian Relations

By Sergei Blagov

Having moved beyond their antagonistic Cold War relationship, Russia and China are now seeking to develop a strategic partnership. In addition to Russia's substantial arms sales to China and the joint military exercises conducted under the umbrella of the Shanghai Cooperation Organization (SCO), the two countries have also sought to cement their bilateral relationship through energy ties. Indeed, China's rapidly growing economy and its increasing demands for energy, combined with Russia's massive energy resources have proven to be a complimentary match. Yet, despite optimistic official pronouncements by the leaders of both countries, thorny issues remain, particularly in the area of bilateral commerce.

Arms Sales and Military Exercises

In recent weeks, a significant number of Chinese soldiers were transported through Russia for the SCO's upcoming military exercises, code-named "Peace Mission 2007." The drill, to be held from August 9-17, involves some 4,000 troops, mainly Russian and Chinese, in Chebarkul, Chelyabinsk region. The Kremlin has made little secret that it views the war games as a demonstration of multilateral solidarity, with anti-Western overtones. In June 2007, the SCO defense ministers met in Bishkek to discuss the drill. At the meeting, Russia's Defense Minister Anatoly Serdyukov criticized the U.S. missile defense plans for Eastern Europe (RIA Novosti, June 27). In an apparent reference to the perceived unilateralism of the United States, he reportedly claimed that some nations used the war on terror and non-proliferation efforts in their own interests, thus undermining the interests of other countries.

These exercises are part of a second series of major joint exercises, with the first being the eight-day maneuvers in August 2005, code-named "Peace Mission 2005," which involved some 10,000 troops in east China's Shandong Peninsula. Repeated displays of Russian and Chinese combined military power were understood to indicate the determination by both Moscow and Beijing to jointly project their clout in Central Asia. Incidentally, the SCO could have marked the "Peace Mission 2007" with even more anti-Western overtones. In 2006, Iran was understood to be interested in participating in the war games under its observer status in the SCO. The June 2006 SCO summit in Shanghai, however, made it clear that membership status was not going to be extended to Iran any time soon. Subsequently, only the militaries from the SCO member-states were invited to Chebarkul in August 2007.

The foundation of the Sino-Russian security relationship, however, rested not as much on the joint military drills, but upon the extensive arms sales between the two countries. Over the past decade, China has been a top importer of Russian-made military hardware, though beginning earlier this year, Russian media outlets have been speculating that Russian arms exports to China, estimated at some $1.5 billion in 2006, were slowing down. Chinese officials were quick to counter these claims. On July 27, Chinese ambassador to Moscow Liu Guchang announced in Chelyabinsk that bilateral military cooperation remained "very successful." In the meantime, Moscow and Beijing have repeatedly pledged to cement their partnership. During his March 26-28 state visit to Russia, Chinese President Hu Jintao hailed what he described as the bilateral "strategic cooperation" and presided over a ceremony in the Kremlin to open the "Year of China in Russia" (Xinhua, March 27).

Energy Partners?

China's import of Russian energy has likewise been a key element in the bilateral relationship, as reflected by the numerous deals that have been struck in recent years. In March, China and Russia signed a joint statement, pledging to cooperate on a variety of issues. In their declaration, Russia and China vowed to boost cooperation in the oil, gas and power sectors in order to consolidate "the comprehensive and long-term strategic collaborative relations in energy and resources" (Xinhua, March 27). Russian state-run oil giant Rosneft and China's Sinopec, however, reportedly postponed signing a $1 billion contract to increase crude oil supplies to China.

In November 2006, Rosneft and Sinopec, a subsidiary of the China National Petroleum Corporation (CNPC), signed an agreement on strategic cooperation. According to Rosneft, joint projects with Sinopec in Russia and some third countries could eventually total $3.5 billion [1].

In July 2005, Rosneft and Sinopec agreed to launch a joint venture to explore the Veninsky deposit, part of the Sakhalin-3 project. In February 2007, Rosneft and Sinopec reiterated their pledges to jointly develop the Veninsky bloc at Sakhalin-3, as well as the OAO Udmurtneft and Adaisky bloc in Kazakhstan. Sinopec reportedly offered to set up a joint refinery venture in Northern China (Interfax, February 7).

In addition, Rosneft, CNPC and the State Development Bank of China have also signed a $6 billion contract, involving the transfer of 50 million tons of crude oil to China. In October 2006, Rosneft and CNPC agreed to set up Vostok Energy, a joint venture company, which planned to produce 10 million tons of crude oil a year by 2009-2010 in Eastern Siberia and Russia's Far East. Rosneft has a 51 percent stake in the joint venture, while CNPC holds the remaining 49 percent interest in Vostok Energy (Interfax, October 17, 2006).

The Kremlin awarded the joint venture with lucrative concessions. On July 31, Vostok Energy placed winning bids to develop two oil and gas deposits in the Irkutsk region (RIA Novosti, July 31). Vostok Energy paid 400 million rubles for a license to develop the Western-Chonsk deposit and 780 million rubles for the Verkhneichersky deposit. On August 1, Rosneft stated that Vostok Energy was interested in a similar auction for licenses to develop the Vakunai and Ignyalin deposits in the Irkutsk region, due in September.

Within Moscow's energy policy, China is clearly a priority, as evidenced by the building of a $12 billion pipeline from East Siberia to the Pacific to pump up to 80 million tons to China and Japan. Furthermore, Russia rushed to build the Eastern Siberia-Pacific Ocean (ESPO) pipeline, despite the uncertainty regarding whether the region could pump enough crude oil to fill it. Russia's pipeline monopoly Transneft pledged to build the 2,694-kilometer pipeline by the end of 2008 (Interfax, July 12). Russian government officials conceded, however, that investments in the ESPO would take 18-20 years to be recuperated.

Russian energy officials sought to reassure their Chinese counterparts that Russia was a reliable energy supplier. Indeed, Russia fulfilled its commitments and supplied 10 million tons of oil to China by rail, Industry and Energy Minister Viktor Khristenko announced in Beijing on July 10 (Interfax, July 9-10). Yet, he seemed reluctant to mention that Russia had previously planned—but failed—to increase its rail-based oil shipments to China up to 15 millions tons in 2006.

Russian officials were also keen to counter questions about the economic viability of the ESPO. The first stage of the ESPO would "undoubtedly" be filled with 30 million tons a year, because Russian oil companies had already pledged so supply more crude oil for the pipeline, Khristenko said in Beijing. If an offshoot to China is built from the ESPO, Russia would supply 15 millions tons/year at the first stage and up to 30 million tons/year eventually, Khristenko said in Beijing on July 10 (RIA Novosti, July 10).

Meanwhile, despite optimistic official pronouncements, indications of disagreements have begun to appear. Khristenko announced in Beijing on July 10 that Russian gas supplies to China may be postponed unless bilateral negotiations on the Western route are completed this year and talks on the Eastern route are finished in 2008. He added that gas supplies along the Western route are expected to start in 2011 and the Eastern route is due to be on stream in 2016 (Interfax, July 10). China, nevertheless, was understood to be reluctant to accept Russian offers of gas at high prices.

In March 2006, Russian President Vladimir Putin traveled to China and pledged to raise oil and gas exports to China. That same month, Gazprom and CNPC signed an agreement on gas supplies from Russia to China, via the "Altai pipeline" of the Western route. Gas supplies via both routes were expected to total 68 billion cubic meters (bcm) eventually, with the first shipments due in 2011. The Western route to China and the Eastern route are expected to funnel 30 bcm/year and 38 bcm/year, respectively.

Although Russia has repeatedly said that its plans to supply China does not mean that oil and gas exports would be rerouted from Europe, Moscow's China-bound pipeline plans are understood to imply a warning to European consumers: Russia would prefer to have the option to redirect oil and gas to China. Yet the Kremlin's pipeline game may still be undermined by China's reluctance to buy Russian energy resources at any price.

Moscow and Beijing also appeared to have struggled to agree on the terms of the ongoing bilateral energy trade. The two countries have long discussed an electricity trade. In the mid-1990s, Russia and China mulled over a project to build a 2,600-kilometer power transmission line from Irkutsk region in Siberia to China at a cost of $1.5 billion. Eventually, however, China abandoned the project in 1999 when the two sides could not agree on pricing.

Nonetheless, Russia has remained interested in exporting electricity to China. Russia's electricity grid RAO UES supplied about 800 million kWh of electricity to China last year and plans to supply 1.4 billion kWh in 2007 (*Vremya Novostei*, February 16). In November 2006, the UES and the Chinese State Grid Corporation agreed to raise annual exports of electricity from Russia to China up to approximately 4 billion kWh/year in 2008-2010, 18 billion kWh in 2010-2015 and 60 billion kWh eventually after 2025 (EDM, July 9).

Earlier this year, however, Russia's plan to boost electricity exports was dealt a major blow. Beginning in February, China refused to import Russian electricity, thus leaving the Bureiskaya and Zeiskaya plants without a market in which to sell electricity (*Vremya Novostei*, February 16). Chinese negotiators reportedly argued that the Russian price of $0.08/kilowatt-hour (kWh) was unreasonable and nearly twice as high as China's domestic prices. On August 3, the UES formally requested the Russian government to approve lower electricity prices in order to resume exports to China.

In spite of these setbacks, Russia reiterated its pledges to develop the energy partnership with China. On July 13, Russian and Chinese Foreign Ministers discussed bilateral ties, including energy issues, during talks in Moscow. After the meeting, Russia's top diplomat Sergei Lavrov noted their mutual interest in investment and energy cooperation, including the coordination of plans to develop Russia's Far East and Siberia, as well as northeastern China (RIA-Novosti, July 13).

Commercial Challenges

Russia has also pledged to increase trade with China, presumably aiming to prop up the bilateral strategic partnership. High growth rates of Sino-Russian commerce have been seen by Moscow as an important indicator of the health of the bilateral partnership. In 2006, President Putin announced plans to raise bilateral trade levels up to $60-80 billion a year by 2010 (Xinhua, March 17, 2006). That same year, Russia's trade with China reached some $30 billion, up 15 percent year-on-year (*People's Daily*, March 27). Russia still sells more goods to China than it buys, but in 2006, Russia's trade surplus was down by 35.4 percent year-on-year at $1.73 billion.

In 2007, Russia's trade with China is expected to reach $40 billion, according to both Russia's Trade and Industry Chamber and the Chinese government (Xinhua, August 1). Russia is no longer expected to have a trade surplus in its commerce with China, however, and growth rates of bilateral trade have begun to slow down.

Furthermore, Russian exporters voiced their concerns over the growing Chinese industrial exports to Russia. In July 2007, Russia's Natural Monopolies Institute (IPEM) released a study, warning of substantial economic and social risks of increased trade with China. The Chinese government subsidizes a number of the country's export-oriented sectors, and subsidized exports could destroy Russia's heavy industry, thus undermining steel production, the petrochemical sector and other industries, the study said. The study suggested that in order to limit Chinese exports to Russia, Moscow ought to increasingly rely on anti-dumping and anti-subsidy investigations as well as technical regulations.

Apart from military and security cooperation, the dynamic development of energy and commercial ties is meant to demonstrate a significant potential for Sino-Russian relations. If the strategic partnership is to become potent, however, many of the disagreements in the commercial relationship, notably ones involving Russian energy exports to China, will have to be resolved.

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Notes

1. See Rosneft press release, available online at: http://www.rosneft.com/news/pressrelease/10614.html.