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China's Quest for Oil in Africa Revisited

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Introduction

Since becoming a net oil importer, the Chinese government in Beijing and its national oil companies (NOCs) have pursued aggressive endeavors to secure oil supplies from Africa. These endeavors often appear to be centrally coordinated, with Beijing's energy diplomacy serving as a forerunner to Chinese NOCs' acquisition of or investment in Africa's oil assets. Together with Beijing's Westphalian norm of sovereignty and non-intervention (essentially a reciprocal principle reflecting and projecting abroad its conception of China's desired politics) as well as Chinese NOCs' alleged lack of interest to engage in best practices, this seeming coordination has raised concerns in Africa and the West. The conventional wisdom has thus far characterized China's pursuit as being orchestrated by the Chinese state to promote the country's developmental interests with little regard for local environmental impacts, revenue transparency, and good governance in the resource-rich continent. Consequently, China is often accused of practicing "neomercantilism" in Africa (Umbach 2007). Because China's quest for oil coincides with the so-called "third wave of democracy" supported by the West across Africa in the aftermath of the Cold War, it is also perceived to run counter to Western efforts to promote human rights and democracy in the continent (Taylor 2006).

This paper takes on the underlying assumptions of the above characterization by disaggregating China into two connected but different actors—the central government of China in Beijing and the corporate China represented by the Chinese NOCs—and accounting for how the "two Chinas" pursue oil interests in Africa. Specifically, it adopts an evolutionary and dynamic approach to demonstrate the following three key variables elucidating the behavior of the "two Chinas" in their quest for Africa's oil. First, the simultaneous convergence and divergence between the interests of the Chinese NOCs and the Chinese government explain the way the Chinese oil giants engage with Africa on oil. Second, Beijing's overarching interests and intentions in Africa, together with the growing imperative for it to promote and protect Chinese NOCs' investment, shape how it promotes and protects China's oil interests in the continent. Third, while host governments of the African oil-rich states have by and large welcomed Chinese oil investment, the "two Chinas" have encountered challenges both at the government level and at the grassroots level, which have led the "two Chinas" gradually to adjust their engagement with Africa.

The structure of this paper is as follows. A preliminary section of the paper places Africa in the broader context of China's global quest for oil. The second section aims to explicate Chinese NOCs' pursuit in Africa. This is followed by an examination of how Beijing promotes and protects Chinese oil interests in Africa. After that, a discussion of how attitudes of host countries shape the way the "two Chinas" engage Africa on oil will be provided. The final section integrates the preceding discussions and draws out both the theoretical and practical policy implications of China's quest for oil in Africa.

Africa in China's global quest for oil

With its oil resource endowment on a per capita basis considerably lower, and its economic growth three times higher, than the global average since 1978, China's transformation into a net oil importer in very short order and its rising dependence on foreign oil is nothing but an inevitability. In view of the compelling economic logic for the country to secure affordable, reliable, and sufficient oil supplies to keep up with its rapidly growing economy, which in turn underpins the legitimacy of the Chinese Communist Party's (CCP) rule, it is natural that the People's Republic of China (PRC)—essentially a party state—attaches high importance to the supply security of its imported oil. But considering that oil is a finite commodity indispensable for every modern economy, the PRC inevitably faces competition in securing supplies overseas from other importing economies. As a late comer on the global oil markets, the country, therefore, has little alternative but to engage in a scavenger hunt for oil worldwide. Because attractive assets have been largely grabbed by Western oil majors that had been operating internationally for a several years by the time Chinese NOCs began their overseas expansion, the "two Chinas" often ended up in places that have unattractive oil assets, high political risks, and unsavory regimes, many of which happens to be in Africa known for being condemned by the typical syndrome of "resource curse" or the "paradox of the plenty."

Africa currently provides about 30 percent of China's total crude oil import and it is the country's second largest source of supply after the Middle East. Three factors have given rise to Africa's prominence in China's global quest for oil. First, the growth of China's oil imports from Africa occurs in tandem with the decline in its imports from the Asia Pacific region as the latter turns into a net oil importer. Africa replaced the Asia Pacific region as China's second largest oil supplier in 1999 and has occupied the position since then. Second, Africa's growing prominence as China's source of imported oil is also an outcome of the country's attempt to diversify away from its dependence on the Middle East, which appears constantly plagued by instability and volatility. Finally, the unique attributes of Africa's oil are another contributor. As opposed to other parts of the world, Africa boasts large untapped oil reserves that are conveniently located for maritime transport, promises outstanding oil reserve growth potential, produces crude oil with low density and sulfur content, remains open to

foreign oil investment, and continues to award production sharing agreements (PSAs) through which foreign oil companies can obtain equity oil (i.e., profit oil after cost recovery). These attributes carry special appeal to Chinese national oil companies (NOCs) because three-quarters of China's refining capacity is designed for crude with low sulfur (Wu 2011).

But the very same attributes also afford Africa's oil a special appeal for other oil importing economies and are responsible for initiating the so-called scramble for the continent's oil at the beginning of the 21st century (Ghazvinian 2007). This makes the oil landscape in Africa very competitive. According to a Chatham House report for the European Parliament, about 500 oil companies are estimated to operate in the continent's upstream oil and gas industry (Baumüller, Donnelly et al. 2011). Thus, Chinese NOCs have to compete with Western oil majors, which have a long established presence in Africa, Western and indigenous independent oil companies, and other Asian NOCs, not the least those from India, Japan, and South Korea (Vines, Wong et al. 2009). To beat out competition and win access, the PRC appears to have adopted a holistic approach that bundles political support, trade deals, debt relief, foreign aid, financial packages, infrastructure projects, and oil deals together in a "business is business" and "no strings attached" fashion. But a deeper look at the respective role of China's NOCs and the government in the country's quest for African oil defeats the myth about a top-down, coordinated, and coherent Chinese oil strategy toward the oil-rich continent.

Making sense of Chinese NOCs' expansion in Africa

To understand China's quest for oil in Africa, one must begin with the country's three major NOCs—China National Petroleum Corporation (CNPC), China Petrochemical Corporation (Sinopec Group), China National Offshore Oil Corporation (CNOOC)—because they are perceived to represent Beijing to carry out oil acquisition and investment activities in Africa. Although Sinochem Corporation, a Chinese oil trading company with upstream ambitions, has acquired some assets in Tunisia, its activities pale in comparison with those by the above-mentioned three Chinese oil giants. Thus, this Paper will concentrate primarily on the three major oil giants. Due to their state ownership structure, the way they acquire and invest in Africa's oil is invariably equated with the intentions and actions of the Chinese state. However, this induction has little empirical basis and is seriously flawed because it fails to recognize the inherent tensions in the Chinese state's bifurcated policy towards its NOCs. Consequently, it exaggerates the convergence (Zhang 2011) but ignores the divergence between the Chinese government and its NOCs both at home and abroad.

The inherent tension concerns Beijing's competing interests regarding oil. With the country's economic growth increasingly dependent upon access to foreign oil, oil security occupies a prominent place on the central government's agenda. However,

concerned that the pass-through effect of oil price volatilities would lead to high inflation and the attendant social instability, it has only liberalized crude oil prices in recognition of China's transformation into a net oil importer but still maintains administrative control over oil product prices at the retail end. In other words, Beijing desires oil security but attaches so much importance to social stability that it is willing to sacrifice the commercial interests of its NOCs. Thus arises the tension between these two objectives.

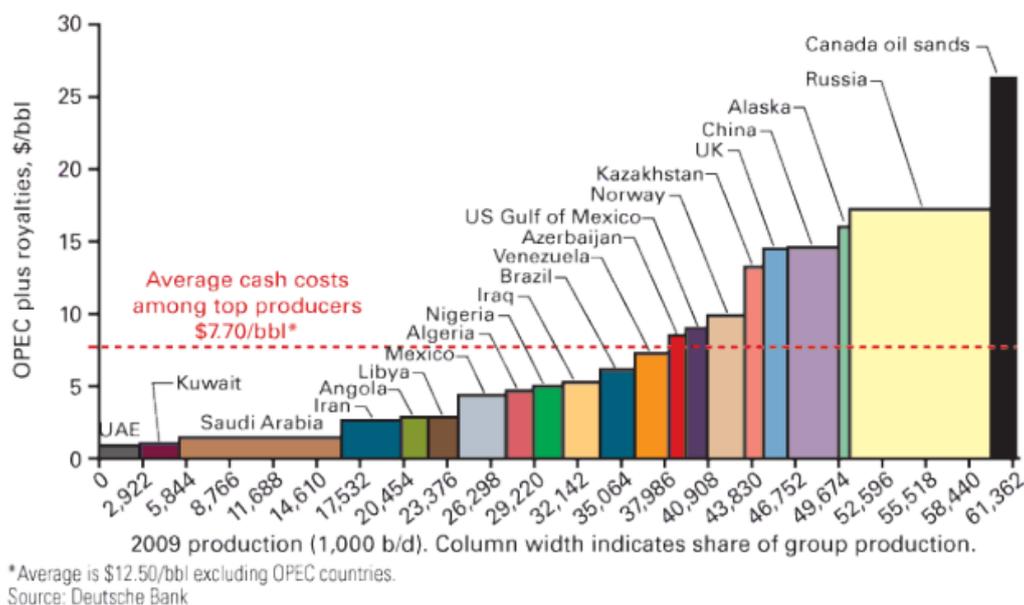
Achieving oil security requires China to have dynamic and vibrant oil companies that can compete on the global oil markets and at the same time liberalize oil prices that can match supply and demand efficiently. This is where the interests of the Chinese government and its NOCs converge. This common interest has driven the central government's endeavor to transform its NOCs through decentralization and corporatization. To foster vitality and competitiveness, Beijing launched decentralization of prices, production, and administration in the oil industry shortly after China embarked on the journey of economic reform and opening up. These decentralizations shifted the locus of most of the decision-making pertinent to oil from the central government in Beijing to the Chinese NOCs. Instead of behaving like state appendages solely responding to central command and control during the era of planned economy, decentralizations have over time afforded Chinese NOCs complete operational autonomy and control over when, where and how they invest and organize their production.

In anticipation of having to open up the country's oil sector when China joined the World Trade Organization (WTO), Beijing also initiated an oil industry overhaul in 1998, which turned all Chinese NOCs into integrated oil companies, broke down the artificial demarcation of their geographical operations and specializations, and liberalized upstream crude oil prices so that the NOCs could reduce their losses and invest for expansion. Moreover, Beijing also forced its oil giants to be listed on foreign and domestic stock markets, thus enabling them to break away from dependence on government funding and raise money from the financial markets for expansion at home and abroad. Having them listed on the New York and Hong Kong Stock Exchange has exposed these NOCs to global rules, norms, and practices. Thus, the domestic overhaul and international public offering further reinforced the direction of the above-mentioned decentralizations and subjected the Chinese NOCs to market conduct. As a result, the restructured-NOCs had to abide by hard budget constraints, divest auxiliary social welfare activities, raise their own funds for investment, and ultimately bear responsibility for their survival and success. They have gained a new identity as profit-oriented corporations subject to market discipline and responsible for their losses and profits.

In contrast, preventing oil price volatilities from hurting vulnerable social groups and leading to intolerable inflation, which could trigger social unrest, requires China to have a tight lid on oil product prices and provide fuel subsidies. However, this leads to

a series of consequences running counter to the objective to enhance energy security. Specifically, fuel subsidies invariably strain state budget; the gap between fluctuating crude oil prices on the global markets and administratively set oil product prices at home often squeeze refineries in China, including those operated by its NOCs, and condemn them to policy-induced losses. Lower retail prices frequently depress incentives for refineries to supply to the domestic market as evidenced by the recent artificial fuel shortages in Southern China, which were caused by opportunistic hoarding in anticipation of price adjustment and oil product being smuggled out of China to neighboring countries for higher prices (Kong 2006). Consequently, administrative controls distort markets, undermine the country's effort to build globally competitive oil companies, and reduce the country's ability to enhance supplies at a time of growing foreign dependence. This is where the interests of the NOCs and the state in China diverge.

Figure 1: Production costs in major oil producing regions (Radler 2009)



This simultaneous convergence and divergence of interests between the NOCs and the Chinese government carry important implications for the Chinese oil giants' quest for oil in Africa. Because of the convergence of interests, the Chinese government has initiated efforts to build competitive oil corporations through granting complete operational autonomy to its NOCs, which made it possible for them take the initiative to seek solutions, including from Africa, to domestic challenges. This is especially true when their mounting challenges at home threatened their survival in the early 1990s and domestic solutions were insufficient. These challenges include maturing oil fields, declining oil production growth rate, rising exploration and production (E&P) costs, mounting debt and welfare burdens, excess oil service and equipment manufacturing capacity in a saturated domestic oil market, and insufficient oil field discoveries (Kong 2010). Meanwhile, China's oil consumption continued to grow and showed no signs of slowing down, which placed the Chinese NOCs under intense

pressure to keep up. This pressure continued to escalate after the country became a net oil importer in 1993. Taken together, these challenges conspired to forge the “push factors” for the Chinese NOCs to look beyond the country’s shores for ways to ameliorate their home-front difficulties. Against this backdrop, the attributes of Africa’s oil and its low E&P production costs, as illustrated in Figure 1, constituted the “pull factors” for the Chinese NOCs to embark on a safari into the continent.

However, Western multinational oil majors have long dominated Africa. Their presence in the continent’s oil industry dates back to the beginning of the 20th century. This extended presence, together with their deep pockets, sophisticated management experience and technological prowess, has provided them with unparalleled advantages in Africa. The oil landscape in Nigeria, the continent’s largest oil producer, provides an illustration. Collectively, IOCs hold 98 percent of Nigeria’s oil reserves (Vines, Wong et al. 2009) and account for 87 percent of the country’s oil production (Tinubu 2010). Similarly, their technological leadership in deep water and ultra-deep water drilling also enables Western IOCs to dominate the offshore oil and gas upstream development in Africa.¹ Hence, IOCs had already captured attractive reserves and quality oil assets in Africa before the Chinese NOCs entered into the continent. Thus, Chinese NOCs had no choice but to go after oil assets shunned by Western IOCs for their depleting reserves or high political risks, such as Civil War or Western sanctions.

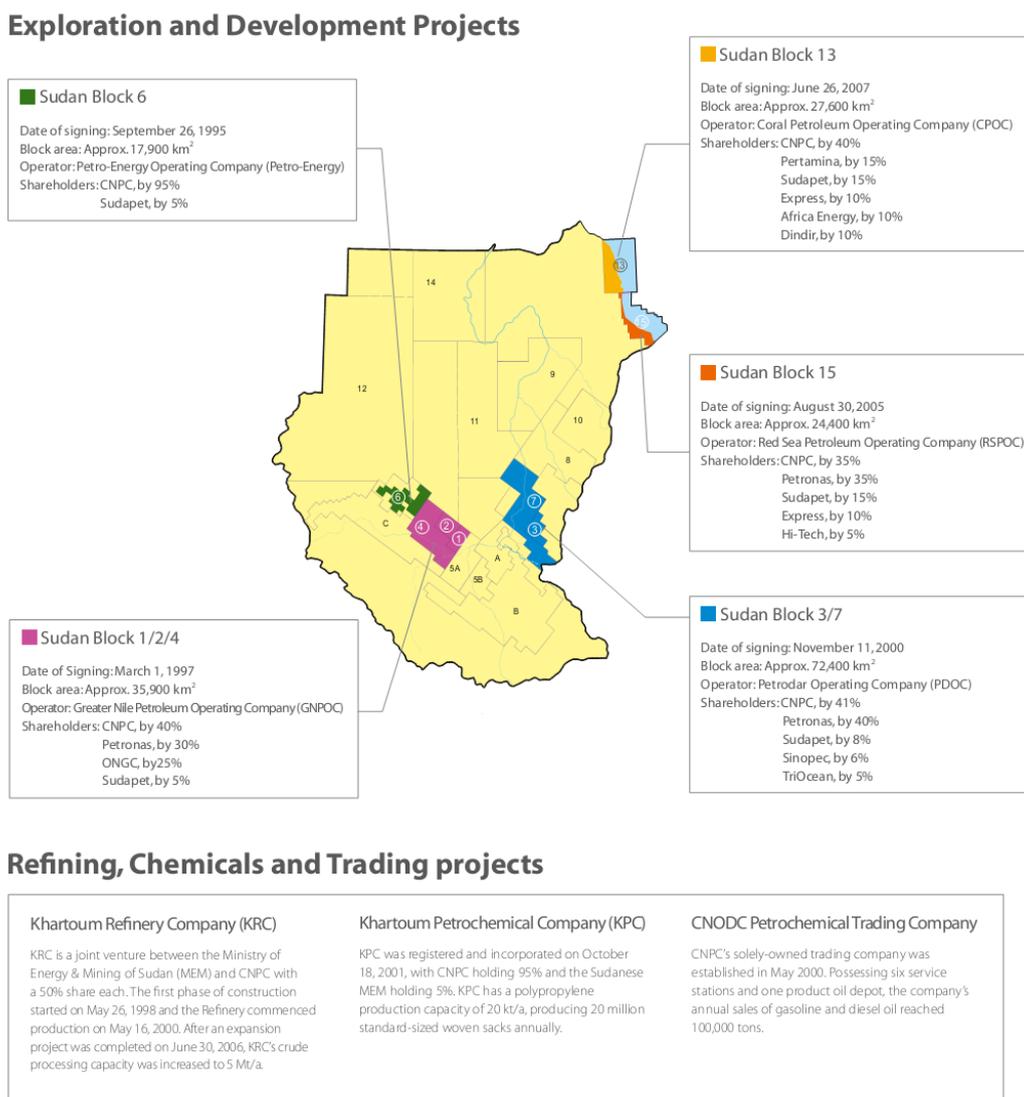
This is illustrated by CNPC’s entry into Sudan, which predated Chinese NOCs’ earnest engagement with Africa. While significant oil reserves were discovered in the country in the early 1980s, its Civil War made operations in the country too risky for IOCs. Chevron, for example, suspended all its operations in Sudan after a rebel group killed three of its expatriate employees in 1984, despite that it had invested, together with Shell, \$1 billion in the country (Kobrin 2004). The American oil company eventually relinquished all of its operations in 1990 amidst the protracted, escalating Civil War that had politicized Sudan’s oil industry. Subsequent U.S. sanctions against Sudan for sponsoring terrorism and violating human rights essentially banned all American oil companies from participating in the Sudanese oil industry.

While the withdrawal of Western IOCs put the Khartoum regime under pressure to look for alternative investment, it presented an opportunity to Chinese NOCs to step up to the plate and fill the vacuum. The opportunity materialized when Omar Al-Bashir, President of Sudan, visited Beijing in September 1995 and requested help with the country’s oil industry during his meeting with Jiang Zemin, then President of China, who then directed CNPC to look into investing into this African country. Based on the conviction that geologies in Sudan are similar to the Bohai Sea in China and that CNPC had the technology and experience in drilling in such geological

¹ Personal communication with Monica Enfield, Director of Research and Advisory of Energy Intelligence, September 13, 2011.

formations, CNPC then signed a PSA with the Sudanese Ministry of Energy and Mines for an oil field (Block 6) in the Muglad Basin in 1995. Thus, at the very outset of its entry into Africa, CNPC demonstrated a higher appetite than IOCs for high political risks. CNPC's entry into Sudan marked the beginning of a sustained expansion, which has culminated in the establishment of an integrated oil production chain (as shown in the Map below), including seven upstream blocs, one refinery, one chemical plant, one oil pipeline, eight gasoline stations, and one oil product storage facility. These projects have put CNPC's investment in the order of \$7 billion (Shi Wei 2011), making oil the defining hallmark of the Sino-Sudanese relationship. Sudan has in turn become a top oil supplier for China and constituted China's largest investment center and equity oil production base in Africa.

Figure 2: CNPC in Sudan (China National Petroleum Corporation 2010)



Emboldened by its success in Sudan, CNPC began to venture into the other parts of Africa, which galvanized the enthusiasm of its competitors at home. With its skill to unlock Africa's oil reserves honed in Sudan, CNPC became much more audacious and

aggressive in expanding on the continent. The recent round of rising oil prices only further fueled the momentum. Beginning from 2003, CNPC expanded into eight more African countries, including Chad, Algeria, Mauritania, Niger, Nigeria, Libya, Tunisia, and Equatorial Guinea. These new adventures involved geological acreages that have no proven reserves and are offshore, although traditionally CNPC only took on onshore projects with proven reserves. Inspired by CNPC's success, Sinopec also made inroads into seven countries—Angola, Algeria, Congo Brazzaville, Côte d'Ivoire, Gabon, Mali, and Nigeria while CNOOC penetrated into five countries—Nigeria, Kenya, Equatorial Guinea, Morocco, and Uganda. Because of this aggressive push, Africa has become the top destination for Chinese oil investment. Between 1995 and 2010, Africa is estimated to have received about \$25 billion Chinese oil investment, eclipsing all other destinations, including Latin America, Central Asia, and the Middle East.² To put this perspective, the three Chinese NOCs collectively have invested nearly \$70 billion overseas by the end of 2010 (Ying Yijie 2011), which means that Africa accounts for 35.7 percent of global Chinese oil investment.

As the Chinese NOCs internationalize their operations the nature of their expansion has gradually experienced some transformation. While it remains essential for them to replace their depleting reserves, find outlets for their excess services and manufacturing capacity (the three Chinese NOCs collectively employ more than 2.3 million Chinese workers), obtain advanced foreign technologies to develop unconventional or deepwater reserves, acquire managerial experiences to engage in large-scale, sophisticated projects (such as liquefied natural gas) at home, international expansion is now an integral part of the Chinese NOCs' strategy to build globally integrated production chain and service the global markets. In this sense, international expansion, including the expansion in Africa, has become a growing source of profit for the increasingly commercially-oriented Chinese NOCs. Indeed, with opportunities constrained at home, overseas activities are increasingly their source of growth. For instance, overseas operations and assets contributed to 27.3 and 31.4 percent respectively of Sinopec's total sales and total assets for 2010 (Li Xingyi and Lei Lei 2011). Thus, with their operational autonomy and the attendant compelling imperative to source profits overseas, the Chinese NOCs have developed a propensity to follow their commercial impulse, which inevitably calls into question their willingness to implement state imperative of supplying domestic markets at commercial losses.

A case in point is how the Chinese NOCs balance energy security for the PRC and their corporate interests. The conventional wisdom on this is that these NOCs follow state imperatives and place priority on China's energy security; as such, they ship their overseas equity oil back. However, empirical studies have proven otherwise. For instance, Sudan constitutes China's largest overseas equity oil production base in Africa, but CNPC actually sells more of its equity oil to Japan and South

² Personal Communication with Kang Wu, Senior Fellow, East West Center, October 3, 2011.

Korea(Rosen and Houser 2007; Ying Yijie 2011). Other Chinese NOCs have done the same with their overseas equity production (Jiang and Sinton 2011). They sell most to the international oil markets. This has been confirmed by a top Chinese NOC executive, according to whom Chinese state-owned oil companies only shipped 5 million tons out of 60 million tons of their equity oil back to China in 2010, meaning that they sold 92% of their equity production to the international oil market (Ying Yijie 2011) . This finding is hardly a surprise given that the nature of local contracts, the intricacies of local politics of the host country, transport cost, and the technical match between crude oil and refining capacity dictate where equity oil can and should be sold. However, this reveals that Chinese NOCs have based their decisions regarding equity oil entirely on a commercial basis, notwithstanding their state ownership and state emphasis on energy security. By doing so, they have actually placed their corporate commercial interests ahead of the pronounced state imperative to secure oil supplies for China. Hence, their behavior in this respect is hardly different from Western oil companies.

This greater emphasis on corporate profits, therefore, suggests Chinese NOCs have become autonomous and self-interested oil companies. Indeed, it is the combination of their autonomy and commercial impulse that gave them the possibility and incentive to begin, expand, and sustain their adventure in the distant but oil-rich Africa since from the mid-1990s. These same traits also prompted them to compete fiercely both at home and in Africa. For example, in 2003 CNPC and Sinopec vied intensely for a pipeline project for Block 3/7 in Sudan and neither side showed restraint even after the PRC Ministry of Commerce pleaded for truce (Kong 2010). Similarly, Sinochem (a primarily state-owned oil trading company with ambitions to become another integrated in China) and CNOOC bid separately for Devon Energy's assets in West Africa in 2007 while CNPC, Sinopec, and CNOOC all bid for Tullow Oil in 2009. Thus, Chinese NOCs' expansion in Africa may have the appearance of an orchestra but there is no conductor that can coordinate the different members.

How Beijing promotes and protects China's oil interests in Africa

The surging dependence of the Chinese economy on African oil, together with the growing Chinese NOCs' oil investment in Africa, calls for the Chinese government to promote and protect the country's oil interests in the continent. But oil interests are merely one dimension of China's interests. Therefore, an understanding of the role of the Chinese government in China's quest for oil in Africa needs to be situated in the broader context of the country's overarching interests and foreign policy intentions in the oil-rich continent. Given Beijing's insistence on the Westphalian norm of sovereignty and its pronounced adherence to non-intervention, a key question for analysis is how Beijing strikes a balance when its oil interests conflict with the other dimensions of the country's interests in Africa or its oil interests come under threat because of host governments' domestic politics.

China's interests in Africa are multifaceted and transcend oil. Broadly speaking, China looks to Africa to secure four dimensions of its fundamental interests. These are: 1) to preserve the country's territorial integrity by preventing Taiwan from expanding diplomatic recognition in Africa and gaining independence; 2) to promote China's economic development interests by sourcing supplies oil, metals, minerals, timber, cotton, diamonds, and other raw materials from the resource-rich continent, and selling its manufactured products to Africa's 1 billion people, many of whom are becoming middle class, which explains China's growing trade with the continent and its replacement of the United States in 2009 to become Africa's largest trading partner; 3) to obtain Africa's diplomatic support at the United Nations for balancing with the United States and Europe regarding issues, such as human rights and climate change negotiations, which in turn raises China's influence in international relations; and, 4) to provide China with a testing ground for the promotion of its newly gained soft power (He Wenping 2007). Taiwan used to dominate the Sino-Africa relationship from the late 1980s and the early 1990s, but now Africa's resources, markets, diplomatic backing, and moral support are what China goes after in its journey to become a great power in the international system. This constitutes the backdrop of Beijing's intervention in Chinese NOCs' quest for oil in Africa.

While oil interests often represent one of the most important dimensions of China's interests in oil-rich African countries, Beijing's policy toward Africa is designed to promote all the above-mentioned fundamental interests. Even in Sudan, where China's oil interests are concentrated and CNPC's oil investment eclipses all other Chinese activities, over 100 Chinese enterprises maintain investment in the country and over 10,000 Chinese participate in its engineering construction (Shi Wei 2011). This explains why Beijing has thrown its support for its NOCs' safari in Africa but this support has come under a broad umbrella of the "going out" strategy. This strategy essentially packages a set of loosely connected policies at home facilitating all state-owned and private companies to engage in overseas investment, foreign construction and engineering contracting, and international service provision. In fact, the other dimensions of China's interests in Africa gives Beijing equal if not more compelling reasons to charm countries in the region with active diplomacy. This active diplomacy frequently takes the form of an integrated approach, which is spearheaded by top-level leadership and bundled together with the provision of trade tariff reductions, foreign aid, low interest loans, debt relief, and investment packages at both the bilateral level and the multilateral level through the Forum on China-Africa Cooperation and China-Africa Summit.

A policy instrument Beijing favors is the "projects-for-oil" approach its state-owned banks pioneered in Angola. Thus, it has become dubbed as the "Angola model." Under the model, Beijing's development banks—the China Export and Import Bank or the China Development Bank—provide concessionary loans tied to the procurement of goods and the participation of contractors from China to help build

infrastructure and social or industrial projects; in return, these oil-rich countries give Chinese NOCs access to their oil resources and repay their loans with their future oil production. Because of its success in Angola, it has been replicated in other parts of Africa, such as Nigeria, Chad, and Ghana, and applied to Chinese acquisition of other raw materials, such as copper in the Democratic Republic of Congo. This approach has inherent attraction for Beijing: it enhances both China's oil interests and other dimensions of interests, such as exports of Chinese goods, services and technology, in Africa. Given the interactions among China's multiple interests in Africa, it is nearly impossible attribute one set of policies to one particular interest. Thus, any attempt to reduce China's interests in Africa to oil or resources is inaccurate and misleading.

The multiplicity and overlap of interests raises an important question about how Beijing strikes a balance when its oil interests conflict with the other dimensions of its interests in Africa. To answer this question, one has to examine Beijing's intentions regarding Africa, which are a derivative of Beijing's overall foreign policy intentions. Despite its rise in the international system and its transformation into the world's second largest economy in very short order, China's engagement with the global system suggest it still remains a status quo power (Johnston 2003). Predicting the exact future intentions of a rising China is tricky because the country's future is likely to be nonlinear and contingent upon the interaction of foreign policy ideas and events (Legro 2007). However, the CCP has made public the two fundamental priorities that will shape China's foreign policy intentions over the first two decades of the 21st century—an important period framed as China's "window of strategic opportunity" by the 16th National Congress of the Communist Party of China in 2002. These two priorities include: 1) the CCP aims to deliver *xiaokang* (moderate prosperity) to China by 2020 through doubling the country's GDP per capita on the basis of 2000 (Hu Jintao 2007); and, 2) the CCP endeavors to lead China to a peaceful rise in the international system (Zheng Bijian 2005), which is later reframed as "peaceful development" to avoid the connotations the realism school of thought tends to attach to the implications of the rise and fall of great powers for peace and stability of the international system.

These two overarching priorities shape and configure the contours of China's foreign policy intentions along two lines. First, despite the country's integration and rise in the international system, its domestic challenges and modernization drive dictate that China will be primarily inward looking. This means that foreign policy will continue to be perceived as an extension of China's domestic policy, which is first and foremost designed to promote country's economic development. Second, the benefits China has obtained from its integration into the international system, together with the future dividends it is likely to gain from its continued, active international engagement, are likely to predispose China to maintain and protect the current international system. This is because China has thus far been one of the biggest beneficiaries of the norms and principles of the rule-based, liberal international order. The ongoing reconfiguration of the international system, which is characterized by the

gradual shift of balance of power in favor of the emerging economies, especially China and India, is likely to deliver more dividend to a rising China and thus further reinforce the country's predisposition to be a supporter and protector of the current international system. More important, this predisposition is consistent with both the compelling incentive for Beijing to construct hospitable external environment conducive to China's fundamental domestic economic agenda and the country's declared commitment to peaceful development. This logical deduction suggests Beijing has no intention to contest the basic rules and principles of the liberal international order; instead it wishes to gain more authority and leadership within it (Ikenberry 2011).

This conclusion carries two import implications for Beijing's pursuit of oil interests in Africa. First, it means Beijing's oil diplomacy is designed to promote China's economic interests rather than change the status of quo of Africa's oil landscape. Indeed, the existing patterns of oil trade and investment in Africa have changed little since Chinese NOCs embarked on their African expansion in 1995. For instance, despite Chinese NOCs' aggressive expansion in the continent and despite Beijing's active oil diplomacy, 41 percent of Africa's oil flew to the United States and Europe in 2010 whereas only 18 percent went to China for the same period (BP 2011). In terms of investment, while Chinese NOCs' presence in Africa has grown significantly in Africa it still pales in comparison with both Western oil majors and African oil companies (Downs 2007). According to the Chinese Foreign Minister Yang Jiechi, total Chinese oil investment only accounts for 6.3 percent of the global oil investment in Africa (Xinhua 2010).

Similarly, the allegation made by Robert Zoellick, during his tenure as Deputy Secretary of the State under the Bush Administration, that China is "locking up" international oil is utterly erroneous and misleading on three accounts: 1) although already the world's second largest importer, China's total oil import only accounted for 12.5 percent of global oil import in 2010 (BP 2011); 2), despite Beijing's active oil diplomacy and Chinese NOCs' aggressive expansion, according a leading energy consultancy Wood Mackenzie, China only has less than two percent of direct access to African oil reserves (Green 2008); and, 3) after years of overseas expansion, Chinese NOCs' equity oil production only reached 1.3 million barrels³, which is less than 2 percent of the global oil production, and the majority is sold on the international oil market, which actually enhances the pie of the global oil market and contributes to the global fungibility of oil. Thus, fears that Beijing's diplomacy will provide Chinese NOCs with unfair competitive advantage crowding out the interests of their Western competitors have not materialized.

Second, the above conclusion also means that Beijing's engagement with Africa is no longer governed by fixation of ideologies as it was during the Cold War era. Instead, it is now primarily based on pragmatism, which first and foremost takes the form of the

³ Communication with Kang Wu, Senior Fellow, East West Center, September 26, 2011

country's economic interests in the continent. In other words, where Beijing strikes the balance if its oil interests are at odds with its other dimensions of interests is *a posteriori* instead of *a priori*. The balance is likely to dependent upon the relative perceived importance of the stakes in question.

The shift in Beijing's stance on the Darfur Crisis and South Sudan's cessation provides a case in illustration. Oil interests, together its Westphalian respect for sovereignty, its longtime foreign policy principle of non-interference, and its philosophy against sanctions, initially prompted Beijing to provide political cover to the Khartoum regime under the National Congress Party (NCP) over the alleged genocide in Darfur at the United Nations Security Council against Western sanctions. However, Beijing's support for and association with the governing NCP subjected it to threats within Sudan from organized opponents of the central state, including the rebel groups in Darfur—the Justice and Equality Movement (JEM)—and in Southern Sudan—the Sudan People's Liberation Army/Movement (SPLA/M); these threats in turn necessitated the imperative need to protect Chinese investment, especially in the oil industry (Large 2009). The repeated attacks by the JEM against Chinese oil workers and the concentration of CNPC's operations in southern Sudan controlled by the SPLA/M drove home to Beijing the point that the Khartoum regime under the NCP had little power to maintain order, ensure stability, and protect China's economic and oil interests in Sudan.

Given the Chinese investment in both Northern and Southern Sudan, Beijing had an incentive to see an end to the continued violence in Darfur and protracted civil war in the South. However, the NCP's pursuit of tactical, defensive maneuvering in a path of resistance ran counter to Beijing's interests in Sudan and the image of “a responsible stakeholder” it tried to present (Large 2009). As the Darfur crisis deteriorated and international pressure on Beijing escalated, especially in the leading up to the Beijing Olympics, it became clear to Beijing that protecting the Khartoum regime had become its liability. Concerned about its international image and compelled by the imperative to protect Chinese investment, Beijing shifted from “quiet diplomacy” to public criticism of the Khartoum regime on the Darfur Crisis and moved from a low-key engagement with the SPLA/M to a public endorsement of the referendum and the subsequent Southern independence. This shift in position on Darfur and Southern Sudan represents a departure from Beijing's staunch support for sovereignty and adherence to non-intervention and provides evidence for its pragmatism when pursuing oil interests in Africa.

Africa responds to the “two Chinas”

China's Westphalian norm of sovereignty and non-intervention gives it a strong preference to engage host governments of the oil-rich countries in Africa in its pursuit of oil interests. This pursuit carries a set of unique features that invariably strengthen

these governments. They include: 1) it helps to drive prices for their oil, as well as other commodities and raw materials, and therefore improve their terms of trade, which had been declining since the World War II until the 2000s (Goldstein, Pinaud et al. 2006); 2) it strengthens their bargaining position as resource providers vis-à-vis other resource or oil investment seekers; 3) it entails noninterference in host countries' internal politics, allowing host governments to perpetuate their style of governance and way of political life; 4) it carries no conditionality whatsoever as long as host governments recognize the principle of "one China," thus prioritizing economic benefits over normative concerns in host countries; and 5) when the "projects-for-oil" approach is employed, it tends to reduce public administration costs required to process the loans and lock host governments into future commitments to build public infrastructure, although the lack of public tender might mean a higher financing costs for host countries (Collier 2008).

The emphasis on infrastructure is especially worth noting given Western donors and international financial institutions have neglected this critical area (Idun-Arkurst and Laing 2007), which constitutes a critical dimension of government function and economic growth. Considering China's growing importance in the international system and the appeal of its economic success to Africa governments, observers in the West often worry that the unique features would help China gain hearts and minds in oil-rich African countries, which would give Chinese NOCs competitive advantages and crowd out Western oil companies. However, the reality is quite mixed. While host governments of oil-rich African countries have by and large welcomed the Chinese oil investment, their engagement with China clearly suggests that there is no evidence of the strong exploiting the weak; instead, these host governments are in the driver's seat and have not uniformly fulfilled their promises. The response to China's pursuit of oil interest in Africa at the grassroots level offers even a sharper contrast. Chinese NOCs have encountered backlash, their workers have been attacked, and they have suffered setbacks in a number of countries. This section aims to account for these mixed responses China has received and how they shape the Sino-African oil engagement.

A key variable explaining African oil-rich host governments' response to China concerns the political nature of these host governments, the basis and the reach of their power in their countries. Most of the oil-rich African countries are essentially petro-states that suffer from the classical "paradox of the plenty" and the "Dutch disease" syndrome (Carl 1997; Ross 1999) . There is often a bifurcation between personal interests for those that govern and the collective interests for those that are governed. Typically, this bifurcation takes the form of oil-rich governments using their discretion to funnel money to support their authoritarian regimes by enriching and empowering their family, friends, military, political supporters, social class, ethnic/religious groups, and specific industries, at the expense of the vast majority of the mass population and the broader economy. As such, the massive flows of petro dollars to these oil-rich countries and modernization of their oil industries only maximize the benefits to a small group of closely-knit elites while leaving the

majority of the society in abject poverty and completely marginalized. This is further compounded by the fact that political power in these oil-rich countries is not so much based on formal institutions as those informal ones, structured along kinship, ethnic, religious, and tribal ties. Consequently, the political power of the small group of elites is inevitably contested within their impoverished societies and the reach of their political power is frequently confined to areas of under their formal controls. Instead of bring prosperity and public wellbeing, the massive flows of petro dollars often stimulate profiteering, rent seeking, corruption, injustice and conflicts.

The above analysis thus suggests a dichotomy of government and grassroots response in Africa to China's quest for oil. At the government level, to the extent China's oil pursuit strengthens oil-rich host governments, they have by and large welcomed Chinese oil investment. This is especially true when the Chinese NOCs, unlike the Western IOCs, have demonstrated willingness to help these oil-rich governments to build modern refineries, which will ease their financial burden on importing oil products from overseas. For example, Chinese NOCs thus far have built or committed to build refineries in quite a few oil-rich countries that have no refining capabilities, including Sudan, Chad, Niger and Nigeria.

However, given that China is neither the top destination for Africa's oil nor the top source for Africa's oil investment, China is actually more dependent on Africa than vice versa when it comes to oil. Thus, host governments in the oil-rich countries are term setters in their engagement with China. While Beijing and its NOCs turn to these governments for diversification of supply, they look for diversification of demand when engaging China. Angola offers a clear illustration. Despite China's provision of a colossal amount of low-interest loans at a time when Luanda needed them badly, there is little evidence supporting the stereotype of weak African states being ruthlessly exploited by the oil-hungry dragon. Instead, the government ruled by the People's Movement for the Liberation of Angola-Labor Party (MPLA) natured its relationship with care and grew its relationship in a pragmatic but disciplined way to the mutual advantage of both countries (Vines, Wong et al. 2009). For example, Sonagol, the state parastatal overseeing oil and gas production on behalf of the MPLA government, scrapped the agreement with Sinopec over the construction of the Lobito Refinery when it became known that the Chinese oil giant wanted to ship oil products to its home market rather than the host country market; as such, Sinopec also had to relinquish the three blocks it acquired amidst Beijing's active diplomacy and promotion of the "projects-for-oil" deals (Vines, Wong et al. 2009; Corkin 2011).

Two recent episodes also further reinforced the signal that the MPLA government remains in the driver's seat of its engagement with China and is set to avoid putting all eggs in one basket. In the first instance, Sonangol blocked the sales of a 20 percent stake of Block 32 from Marathon to CNOOC and Sinopec in September 2009 and in the second instance the MPLA government reached an agreement with the International Monetary Fund (IMF) on a loan for \$1.4 billion in November 2009. The

second instance was especially significant and telling about the MPLA government's intentions given the worries about China's "projects-for-oil" deals increasing Angola's debt burdens and discouraging Angola from turning to international financial institutions. Similar stories have also been repeated in Libya when the Qadhafi government blocked the sale of Verenex, a Canadian firm predominantly holding oil assets in the country, to CNPC for around \$415 million and in Ghana where the government did not award Chinese NOCs upstream opportunities despite their aggressive pursuit.

Further, the bifurcation of interests in oil-rich countries, as mentioned above, frequently motivates ruling elites to seek petro dollars and their associated development dividends for personal gains, thereby subjecting China to the whims of the mercurial politics in these oil-rich countries. Nigeria provides a case in point. Ostensibly to reduce dependence on Western IOCs that are dominant in Nigeria's oil landscape but reluctant to build downstream and infrastructure projects, President Olusegun Obasanjo launched an aggressive initiative to secure investment from Chinese NOCs, together with other NOCs from India, Taiwan, and South Korea, into the country's infrastructure projects in return for oil block concessions he would grant on highly favorable terms between 2005 and 2007 before his tenure was to expire. Eager to gain access to upstream opportunities in the top African oil producer, the Chinese government and its NOCs took the bait and signed onto "oil for infrastructure" projects promoted by the Obasanjo government after the fanfare of bilateral top leadership visits and amidst Western worries about being crowded out. However, the Obasanjo government's failure to put in place a formal mechanism to enforce these deals, combined with its hidden agenda to generate funds for President Obasanjo's (ultimately unsuccessful) bid to change the constitution to allow him to run for a third term, foretold the collapse of these deals (Vines, Wong et al. 2009).

President Umaru Yar'Adua, Obasanjo's successor, reversed and cancelled many of the deals, including those signed by Chinese NOCs and brokered by the Chinese government during the last three years of the Obasanjo era either because they were not deemed to be in the national interest or because of the discovery of large-scale corruption in the execution and non-execution of projects. Thus, except for Sinopec's acquisition of Canada's Addax Petroleum for \$7.2, Beijing and Chinese NOCs' pursuits have not yielded noticeable success.

While the elites of oil-rich countries have by and large welcomed Chinese oil investment, those marginalized by the globalization of Africa's oil industry and opposed to the oil-rich governments often see China's pursuit in a different light. They tend to view China's support for and association with their oil-rich governments as a reason that perpetuates the injustice and conflicts fueled by the ruling elites' theft and abuse of their oil wealth, to which they are denied of access by their authoritarian, corrupt, and opaque governments. Thus, they often redirect their animosity and hostility against their governments to the "two Chinas." Attacks of Chinese oil

operations by rebel groups fighting for their rights over oil and opposed to oil-rich governments in Ethiopia, Sudan, and Nigeria illustrate this different response the “two Chinas” get from oil-rich Africa. For example, the Ogaden National Liberation Front (ONLF), a separatist rebel group fighting to make the region of Ogaden in eastern Ethiopia an independent state, attacked a Sinopec subsidiary for conducting oil exploration in the region and killed nine Chinese oil workers in April 2007. Abdirahman Mahdi, a spokesman for the ONLF in London, told the BBC's Focus on Africa program "We have warned the Chinese government and the Ethiopian government that... they don't have a right to drill there. Unfortunately nobody heeds our warning and we have to defend our territorial integrity" (BBC 2007).

Similarly, after attacking CNPC's oil operations in Block 4 in Kordofan (see Figure 2) in October 2007 the Darfurian rebel group JEM announced “this is a message to China and Chinese oil companies to stop helping the government with their war in Darfur” (Reuters 2007). This was followed by another rebel attack against CNPC operations, which resulted in the killing of five out of nine abducted Chinese oil worker in Southern Kordofan near the Abyei region, an oil-rich flashpoint area in a contested border zone between Northern and Southern Sudan. To warn Chinese oil companies against expansion into the Niger Delta, the Movement for the Emancipation of the Niger Delta (MEND) detonated a car bomb close to the Warri oil refinery, which coincided with the visit of the Chinese President Hu Jintao to Nigeria and the granting of four (ultimately collapsed) oil drilling licenses valued at \$4 billion. In the email it sent to media organizations around the world, MEND said “We wish to warn the Chinese government and its oil companies to steer well clear of the Niger Delta. The Chinese government by investing in stolen crude places its citizens in our line of fire” (BBC 2006). However, it would be erroneous to over-interpret these attacks. After all, Western oil companies, especially those operating in the Niger Delta, have long been experiencing militia attacks and there is little evidence of coherent and systematic hostility to China in Africa.

The “two Chinas” progress through a rapid learning curve

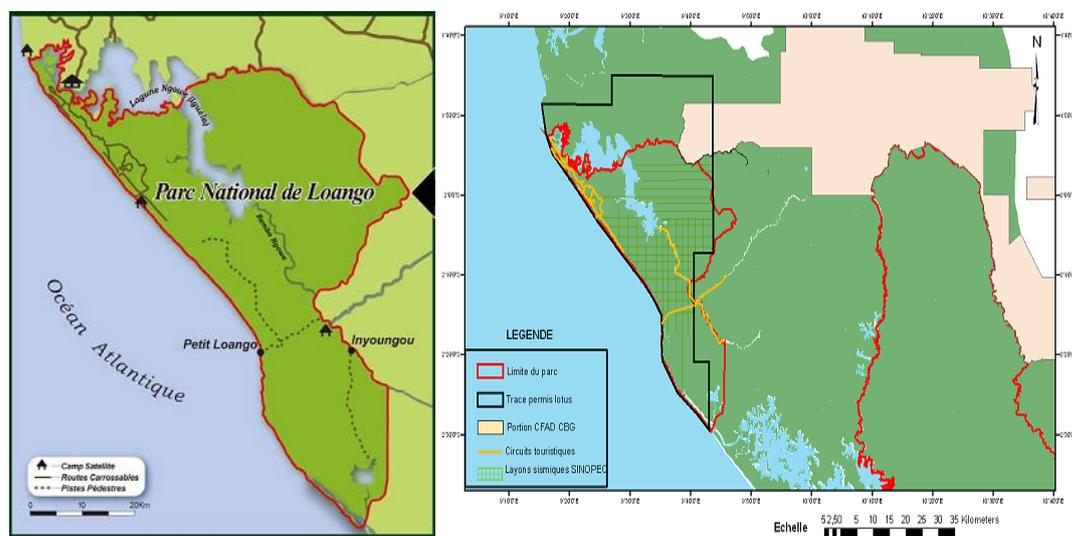
Nevertheless, this dichotomous response highlights the delicate challenge for the “two Chinas” to protect their oil interests in conflict zones in Africa and prompts adaptive learning. Essentially, the “two Chinas” face a conundrum—their access to Africa's oil depends on their relationship with the oil-rich governments but it is this relationship that often subjects China's oil interests in conflict zones to attacks by opposition or marginalized groups. Further, the assumption that these governments, like the one in Beijing, possesses the capability to maintain order, ensure security, enforce contracts, and protect China's oil interests does not hold. This means many of these oil-rich governments lack the capability to protect China's oil interests. This asymmetry of political power between formal institutions and informal institutions means that both the “two Chinas” have to adapt their behavior based on the respective strength and

limits of these institutions.

This recognition has induced some behavioral change of the “two Chinas” in their engagement with Africa on oil. At the government level, Beijing has demonstrated pragmatic flexibility in its Westphalian norm of sovereignty and non-interference. With the growing imperative for it to protect Chinese oil interests, among a variety of other interests, in Africa, Beijing has modified and moved away from its dogmatic foreign policy principle in both Sudan and Libya by engaging opposition forces and establishing diplomatic ties with them once they establish formal control and gain international recognition. Beijing’s positive, albeit belated, role in resolving the Darfur Crisis and the cessation of South Sudan has won it international praises and raises hope about Beijing embracing “the responsibility to protect” and the “duty to respond” thesis that have been promoted by the U.S. and Europe.

At the corporate level, the Chinese NOCs have shown propensity to adapt and embrace best practices. Sinopec’s experience in Gabon provides a case in point. Supported by the Gabonese Ministry of Mines, Energy and Petroleum, the Chinese oil giant started to conduct seismic activities in the Loango National Park (see Figure 3&4) using rudimentary methods and before implementing the appropriate environmental impact assessment (EIA). This violated both the regulations required by the Gabonese Ministry of Forestry and National Parks Administration and also the Gabonese government’s legal agreement with the Global Environment Facility Trust Fund and the World Bank, which allowed the World Bank to execute an investment of \$10 billion into the Loango National Park (Center for Chinese Studies 2007). As such, the World Bank, together with conservations groups based in Gabon, such as the World Conservation Society (WCS) and Brain Forest, managed to halt Sinopec’s activities despite the Chinese and Gabonese government resistance. Faced with this pressure, the Gabonese government invited the World Wildlife Fund (WWF) and WCS to audit Sinopec’s exploration activities against the environmental and social protection stands they have developed and asked Sinopec to accept collaboration with these non-governmental organizations (NGOs). According to James Deutsch, director of the WCS’s Africa Program, the WCS-WWF managed to build construct partnership with Sinopec, which allowed its audit team to move into Sinopec camps, sensitize Sinopec staff to agreed standards and protocols, and achieve positive results (Deutsch 2010). While Sinopec completed exploration in the Loango National Park, finding too little oil for terrestrial extraction to be commercial, it clearly demonstrated its intention to adopt best environmental practices. In fact, the World Bank even maintained that the current stands used by the Chinese company are now higher than those imposed by international conventions (Center for Chinese Studies 2007).

Figure 3&4: Sinopec's operations in Loango National Park (Deutsch 2010)



Similarly, Chinese NOCs have also followed the footsteps of the Western oil companies in voicing support for human rights and embracing corporate social responsibility (CSR). For example, the publicly listed subsidiaries of all three Chinese NOCs signed up respectively in 2004, 2007, and 2008 for the United Nations Global Compact, which commits businesses to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labor, environment and anti-corruption. Similarly, all three Chinese NOCs now publish CSR-related annual reports at home, with CNOOC setting the trend in 2005 and CNPC and Sinopec following suit in 2006. They also incorporate CSR into their operations in Africa. For example, by 2009, CNPC, through its subsidiaries and joint operating companies in Sudan, had donated nearly \$50 million to local charity groups and neighboring communities around oil blocks and beginning 2010 it will donate to charity \$1 million every year for three consecutive years (China National Offshore Oil Corporation 2010; China National Petroleum Corporation 2010). Conscious of the need to promote localization, CNPC employs 6,700 people in Sudan, among whom local hiring accounts for 95 in its upstream projects and 75 percent in its engineering service projects (China National Offshore Oil Corporation 2010).

If measured against the voluntary embrace of the United Nations Global Compact and CSR, Chinese oil companies are not much different from Western oil companies. Despite being positive, the significance of NOC behaviors for the improvement of good governance, revenue transparency and public wellbeing in the region should not be exaggerated. After all, the presence of Western oil companies, which embraced these standards long before their Chinese counterparts, in Africa has not changed the volatile situation in the Niger Delta, the coexistence of massive oil flows and abject poverty in Angola, or the classical manifestations of the “resource curse” in Equatorial Guinea. In other words, oil companies, Chinese or Western, are not a force

that one should expect to deliver the antidote to the “paradox of the plenty” or bring about good governance and public accountability (Pegg 2011). It is ultimately onerous upon the oil-rich governments in Africa to hold all foreign oil companies accountable. But this should not exonerate Beijing from the responsibility for regulating its NOCs and holding them accountable for their behavior in Africa. Given the capacity decay Beijing has experienced in the era of reform, as manifested by the severe bureaucratic fragmentation within the central government of China, the rise of the Chinese NOCs and local governments in energy affairs (Kong 2011), Beijing, like the oil-rich governments, also need to improve its regulatory capacity.

Practical and theoretical implications

Despite China’s aggressive pursuit of oil interests in Africa for the past 16 years, misperceptions and misinterpretations still abound. This paper contributes to the literature by separating China into two structurally connected but inherently different actors and defeats three prevailing myths. First, the “two Chinas” have simultaneous convergence and divergence of interests and it is this dichotomy that explains the paradox of Beijing’s support for its NOCs and its NOCs’ reluctance to ship their equity oil in Africa back home. Second, the rising dependence of the Chinese economy on African oil and Chinese NOCs’ growing investment in Africa have conspired to create an imperative for Beijing to promote and protect Chinese oil interests; given Beijing’s multiple interests and pragmatic intentions in Africa, how Beijing might strike the balance, however, is rarely *a priori*. Third, in its engagement with Africa, China is a term taker not term setter and the dichotomous response it has encountered has changed how the government of China and the Chinese NOCs engage Africa on oil. Thus, it is erroneous to label China’s quest for oil in Africa as “neomercantilism” or “neocolonialism.” The existence of these very misperceptions and misinterpretations has much to do with flawed assumptions and lack of nuanced understanding, but it is attributable to the lack of transparency about how the “two Chinas” actually engage with Africa on oil.

Thus, one practical implication of this Paper relates to the need for information disclosure by the “two Chinas” on their quest for oil in Africa. Information disclosure by the “two Chinas” will help quell apprehensions and concerns about their intentions and impacts on the international oil market, Western NOCs, and host countries. The Chinese NOCs’ recent embrace of the United Nations Global Compact and CSR is a positive development that could lead to more information disclosure, which could also assist civil societies and NGOs in Africa to hold their governments accountable. However, one should refrain from holding out high hopes about the Chinese NOCs, and for that matter oil companies of any national origin, becoming a positive force for providing cure for poor governance and opaque revenue transparency in oil-rich countries. For their chief concern were, remain, and will continue to be their corporate balance sheet. To the extent they engage in CSR activities, they are designed to

facilitate their profit maximization and are an outcome of a variety of developments, including the spillover of domestic practices responding to domestic pressure and regulations, grassroots demands, international pressure, and most importantly demands from oil-rich African governments. Unfortunately, these governments have yet to step to the plate and play a more positive role in promoting good governance, accountability, and revenue transparency. This inevitably raises questions about the incentive, interests, and intentions of the governments in oil-rich African countries.

The findings of the Paper also raise theoretical questions that need further research. As explained earlier, both the oil-rich governments in Africa and Beijing need to improve their regulatory capacity to maximize benefits and minimize the unintended consequences of their engagement. However, at this point it is not clear what improved regulatory capacity means for the oil-rich African countries and China. For the former, the following questions need to be answered: How do oil-rich governments regulate foreign oil companies? What determines the scope of their regulation? What are the interest and incentives in their regulation? Do they represent the public interests? For the latter, further research is needed to answer the following questions: If the government of China improves its capacity to regulate its NOCs, what will it do to the convergence and divergence of their interests? Will that run counter to the country's domestic price interests? How will it change Chinese NOCs' behavior in Africa? How these issues play out will shape future of oil engagements between the China and Africa.

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