Quest for Oil and Geostrategic Thinking

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The production levels of oil and gas in China, India and the United States are either in decline or have stagnated. Meanwhile, the level of energy usage has dramatically risen in these countries. This has created a deficit between local production and domestic usage which in turn, has to be covered through the import of oil and gas. However, the search of such overseas energy resources is increasingly taking on a competitive streak. Tension has been building, especially in Asia, as the race to secure oil and gas abroad heats up.

In a recent article in *Alexander's Oil & Gas Connections* titled "United States and China are after oil sands," we learn that both Chinese President Hu Jintao and U.S. Treasury Secretary John Snow used their visits to China to discuss the oil fields of Alberta, which is said to contain the world's largest reserves of oil sand. These fields are estimated to contain 180 billion barrels of oil, second only to Saudi Arabia's reserves of oil.[1] Chinese growing interest in Canadian oil sands is further illustrated by China Petrochemical Corporation's deal with Calgary based Synenco Energy to buy 40 percent of the Northern Lights oil sands project, and China National Offshore Oil Corporation's (CNOOC) purchase of a 16.69 percent stake in MEG Energy.

Relations between China and America frayed again when China National Petroleum Corporation's (CNPC) attempt to purchase Unocal, America's ninth largest oil company, earlier this year was rebuffed with American Congressmen voicing strong opposition towards this Chinese bid. Former CIA director James Woolsey even went as far as to describe the Chinese attempt as "a threat to U.S. national security."[2] The angry reaction in the U.S. Congress came at a time when U.S.-Venezuela relationship was going through a difficult patch. Venezuela is the fourth largest supplier of oil to the U.S., catering to about 11 percent of America's oil needs. However, President Hugo Chavez of Venezuela

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[1] *Alexander's Oil & Gas Connections* 10, 19, October 11 2005, <http://www.gasandoil.com/goc/news/nts54124.htm> (November 1 2005).

[2] *Alexander's Oil & Gas Connections* 10, 18, September 28 2005, <http://www.gasandoil.com/goc/news/ntn53958.htm> (November 1 2005).

who is anti-American has been threatening to cut the U.S. off Venezuelan oil. Such a move, if carried out would most certainly cause serious damage to U.S. energy security. Chavez' rationale is mainly political—to show that he could stand up to U.S. power in South America. He has gone as far as expressing interest in cooperating with Argentina, Brazil and possibly Iran to develop nuclear energy. As part of his bid to counter U.S. influence in Latin America, he invited China to replace the U.S. as recipient of Venezuela's oil.[3] China's cautious but nevertheless positive response further annoyed the U.S. Congress and such emotions became apparent during the debates on the Chinese's bid for Unocal.

Quest for Oil Initiating State Competition

U.S. oil reserve additions have only managed to replace 58 percent of crude oil production in 2003, a trend observed since the early 1990s.[4] Furthermore, with declining crude oil production and the inability to meet rising domestic demand, the U.S. has grown increasingly dependent on energy imports. Such reliance has been forecasted to grow by 2.5 percent annually until 2025.[5] From an American point of view, the rising energy demand has not been a problem in the past. However, competition in the energy market has risen significantly due to the greater international demand for oil.

The problem is a global one, with much of its roots in Asia. According to the International Energy Agency,[6] primary energy demand in the world will increase by 66 percent from the year 2002 to 2030. Asia's share will increase from 28 percent to 35 percent. The share increase will be especially significant with regards to oil demand. The Asian developing countries will take the largest share, 38 percent in 2030, with China taking 16 percent and India 8 percent.[7]

China is at present experiencing an energy supply crunch; one that is so severe that the government has ordered the slow down of investment in oil-intensive industries. China's energy shortages are very much linked to

[3] *Alexander's Oil & Gas Connections* 10, 3, February 10 2005, <http://www.gasandoil.com/goc/news/ntn50617.htm> (November 1 2005).
[4] US Energy Information Administration, US Dept. of Energy, Energy Statistics, U.S. Crude Oil, Natural Gas, And Natural Gas Liquids Reserves (Annual Report 2003), 21.
[5] US Energy Information Administration, US Dept. of Energy, Energy Statistics, Data.
[6] IEA-India Workshop on Emergency Oil Stock Issues, *Opening Remarks by Ambassador William Ramsey, Deputy Executive Director of the IEA*, <http://www.iea.org/> (February 9 2005).
[7] IEA-India Workshop on Emergency Oil Stock Issues, *Opening Remarks by Ambassador William Ramsey, Deputy Executive Director of the IEA*, <http://www.iea.org/> (February 9 2005).

its modernization process. Two major factors are said to be the cause of China's energy shortages. First, and most important, is the growing affluence of the Chinese population. With rapid GDP growth, living conditions have improved and an increasingly significant portion of the population can now afford to purchase cars, and electrical appliances such as air-conditioners, refrigerators and heaters. The second cause is the lack of investment in the coal sector. Coal has traditionally catered to two-thirds of the electrical energy consumed but of late, has increasingly been unable to keep up with the rising demand for electricity. As a result of growing energy demand and the inability of the traditional coal sector to keep up with supply, the importation of oil has been increasing rapidly. Between 2002 and 2003, the rate of imported oil increased by 44 percent. If China's demand for oil imports continues to grow at this rate, the oil market will have difficulty meeting its requirements.[8]

In 1990 China took most of its crude oil imports from nearby friendly-countries. However, a decade later, China's increasingly urgent quest for energy supplies has forced it to look further beyond. In 2001, China's international investments included several Middle Eastern countries, Argentina, Bangladesh, Canada, Colombia, Ecuador, Indonesia, Kazakhstan, Malaysia, Mexico, Mongolia, Nigeria, Pakistan, Papua New Guinea, Peru, Russia, Iran, Sudan, Thailand, Turkmenistan, Venezuela and the Gulf of Mexico. Altogether, the China National Petroleum Corporation (CNPC) had signed or was in the process of negotiating, contracts in at least 20 countries. It also pledged more than $8 billion in exchange for oil concessions in Sudan, Venezuela and Iraq.[9] During the last four years, China has also invested in large projects in Brazil and Canada.

Compared to China, India is a late-comer in the race for oil fields abroad. It is basically facing the same problem as China where the pace of modernization processes is outstripping energy demand. India's energy import statistics is very telling. Oil imports increased by 6.3 times between the 1970-2002 period while domestic production only increased by 4.5 times. This makes India's import dependency as high as 73.3 percent in 2002. As dependence on overseas supply grow, state-owned Indian oil companies have also become active in the quest for energy security.

Under the pressure to improve oil import security, the state-owned Oil and National Gas Corporation (ONGC) has acquired exploration blocks abroad in Myanmar, Sudan, Iraq, Russia, Vietnam, Venezuela and Libya. It has also begun a deep-water drilling program in the Bay of

[8] *Alexander's Oil & Gas Connections* 9, 17, 2004, <www.gasandoil.com/goc/frame_cns.company.htm> (September 21 2004).
[9] *Ibid.*

Bengal. The private sector company Reliance Industries Ltd is pursuing a plan for equity and acquisition of oil fields in Sudan, Iraq, Madagascar and Libya and has a stake in an exploration block in Yemen.[10]

Chinese and Indian Energy Diplomacy Worries the U.S.

It seems that the U.S. is genuinely concerned about the long-term consequences of competition with the two Asian giants. America's growing unease towards the two Asian powers was reflected in the report titled "Mapping the Global Future" published this year by the U.S. National Intelligence Council, a government think-thank which advises the Central Intelligence Agency and senior U.S. policy-makers. The report states that "the likely emergence of China and India as new major global players...will transform the geopolitical landscape". It adds that "in the same way that commentators refer to the 1900s as the 'American Century,' the early 21st century may be seen as the time when some in the developing world, led by India and China, come into their own.....(and) will have substantial impacts on geopolitical relations."[11]

It was reported that Deputy Secretary of State Robert Zoellick in a visit to Beijing, told his Chinese hosts that "China will be increasingly in conflict with the United States if it continues to pursue relations and energy deals with countries the U.S. believes to be "problematic."[12] Henry Kissinger even warned that "the global battle for control of energy resources could become the modern equivalent of the 19th century 'Great Game' between Great Britain and Tsarist Russia for supremacy in Central Asia."[13]

China's quest for energy has also created problems in its near abroad. The Sino-Japanese dispute over oil and gas discovered offshore in the East China Sea, their rivalry over the pipeline route from Angarsk in Russia, and competition for the oil riches of the Sakhalin peninsula are all potentially destabilizing elements for the two countries' relationship.[14] China's influence in the Central Asian states and particularly Kazakhstan are also growing in significance as plans are underway to link

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[10] Reliance, Exploration & Production (Oil & Gas), <http://www.ril.com/business/petroleum/ep/business_petroleum_ephome.html> (September 20 2005).

[11] *Alexander's Oil & Gas Connections* 10, 15, August 17 2005, <http://www.gasandoil.com/goc/news/ntn53306.htm> (November 1 2005).

[12] *Alexander's Oil & Gas Connections* 10, 18, September 28 2005, <http://www.gasandoil.com/goc/news/nts53990.htm> (November 1 2005).

[13] *Alexander's Oil & Gas Connections* 10, 12, June 22 2005, <http://www.gasandoil.com/goc/news/ntn52546.htm > (November 1 2005).

[14] Ingolf Kiesow, *China's Quest for Energy; Impact upon Foreign and Security Policy*, (Report at the Swedish Defence Research Agency, FOI-R--1371—SE, 2004) <www.asia.foi.se> (November 1 2005), 41.

the two countries via an oil pipeline. However, the pipeline also represent a breach of Russia's monopoly-like control of oil and gas exports from Central Asia, something Russia is not to be too happy about.

Just like China, India's energy diplomacy has also encountered problems with the United States. Together with neighboring Pakistan, plans are now underway to build a $7 billion gas pipeline from Iran. This did not go down well with the U.S. who pressured New Delhi to abandon the plan. In fact, U.S. pressure did not stop India from making another deal with Iran, this time, to import 5mm tons per annum of liquefied natural gas (LNG). The deal is valued at close to $22 billion and is the largest commercial deal ever entered into by India in the hydrocarbon sector. As a follow-up, a special envoy was sent by Iran to propose a comprehensive economic and political cooperation agreement. The idea of energy security cooperation between India and Iran is obviously a matter of significant concern for Washington as President Bush took up this issue with Prime Minister Manmohan Singh during talks on the sidelines at the opening of the UN General Assembly session in New York in September 2005.[15]

Energy Efficiency and Lessons to Learn from History

In an article by two prominent oil experts in the *Far Eastern Economic Review* an interesting observation is made. It states that the ruling party in China is, "...running the financial system primarily for the benefit of its own constituency of companies...With its economy requiring more oil per unit of output, China's emergence as a global economic powerhouse has caused the world economy to become more oil intensive...Whether the recent relinking of growth to rising oil intensity is the beginning of a new trend led by China or represents just a temporary phenomenon is one of the key uncertainties for the global energy markets going forward."[16] The article argues that "Improving energy efficiency is becoming a key driver of energy policy, and greater diversification of foreign suppliers as well as the energy mix looks set to gather momentum." This is the approach of the economists and engineers to the rapidly emerging problem of high oil prices due to declining production rates in combination with rapidly rising demand in some of the main consumer countries. This certainly represents a necessary insight in the "need to do something", but it can also become a dangerous decision trap. The problem is not only one of system engineering. The more dangerous side of the problem is the tendency towards geostrategic thinking that has

[15] *Alexander's Oil & Gas Connections* 10, 18, September 28 2005, <http://www.gasandoil.com/goc/news/nts53977.htm> (November 1 2005).
[16] Peter Cornelius and Jonathan Story, China revolutionizes Energy Markets, *Far Eastern Economic Review* 168, 9 (October 2005): 21.

appeared so conspicuously in the U.S., China and to a certain extent also in Japan, India and Europe.

We have some examples in history to remind us of the dangers that is hidden in that kind of reasoning. Adolf Hitler's original plan for the attack on the Soviet Union in the summer of 1941 had as one of the two most important parts a push through southern Ukraine in order to get secure access to the oil fields in Baku. To secure the supply of oil for the German forces and to cut off the Soviet supply seems to have been an important reason for his opening of a second front.[17] In September 1941 Japan's leaders decided to go to war with the United States if an agreement regarding oil was not reached by early October. Since an American oil embargo against Japan, which had been introduced in July, was still not lifted in October, plans for war were made and on December 7 the Japanese fleet attacked Pearl Harbour.[18] In July 1990 I happened to become an eye-witness to the failure of the last negotiation in Basra between Iraq and Kuwait about border issues, among them the oil fields on the border between the two countries, and about the OPEC price level for oil that were the two main factors behind Saddam Hussein's decision to invade Kuwait two months later, on August 1.[19]

It is not geostrategic thinking itself that is a decision trap. Oil is becoming a more scarce resource, compared to demand, and it is time to start not only one but both available lines of action, to improve energy efficiency and to secure supply of oil. Since the world is still a set of nation states, any government who neglects the geostrategic aspect is likely to be criticized by its citizens—and rightly so. It is the solution to the geostrategic problem that represents the danger. It is wrong if every nation starts to grab as much oil as possible without regard for the needs of other nations. The goal must be to create an efficient world-wide structure for oil production and a network of distribution that can give all nations as much oil as long as possible at the same time as energy efficiency is increased and to do so in a way that energy is produced by other means than by the burning of more oil. That requires international cooperation on a grand scale, not mercantile theory reflexes.

The academic world now has a task to alert politicians and public opinion to the growing energy problem. Since there is an obvious need for geostrategic thinking, whether we like it or not, the alert should also

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[17] Hermann Rausching, *Gespräche mit Hitler,*Zweite Auflage (New York: Europa Verlag, 1940), 120-127; Werner Maser, *Adolf Hitler; Legende-Mythos-Wirklichkeit* (Muenchen: Wilhelm Heine Verlag, 1975), 499-503.

[18] John K. Fairbank, Edwin O Reischauer and Albert M Craig, *East Asia; Tradition and Transformation* (London: William Clowes & Sons, 1975), 717-720.

[19] Ingolf Kiesow, *Svensk Kuwait* (Stockholm: Probus förlag, 1992), 28-30, 46 and 48.

highlight the inherent danger of the wrong approach to such thinking. The latter task is probably the most important one—and the most difficult and unrewarding one.