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Is China's outward investment in oil a global security concern?

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The motivations prompting China's dramatic increase in outward foreign direct investment (OFDI) are not always clear, especially regarding OFDI by state-owned enterprises (SOEs) in energy and natural resources. First, both commercial and governmental interests are intertwined, although not necessarily in lock-step. Chinese SOEs listed in the West may worry about the reputational risks to their global corporate citizenship, while government stakeholders may instead focus on diplomatic international relations. Second, subsidies for oil investments may be viewed as serving Chinese national interests and threatening the national security of the host countries. Whether China's OFDI will benefit or harm global energy security, economic development and diplomatic relations is still hotly contested.

China is acutely concerned about the security of its oil supplies. In the 1950s, the newly established People's Republic of China was at the mercy of the Soviets for oil. The Sino-Soviet split in the 1960s led to critical oil shortages and jeopardized the Chinese military. The Daqing Oilfield production starting in 1963 gave China temporary independence from oil imports. However, due to the depletion of Daqing and rising domestic consumption, China again became a net oil importer in 1993, sparking old anxieties and precipitating China's national goal "to provide reliable and adequate supply of oil [to the Chinese people] at a reasonable price."[1]

Each of China's three oil-related objectives -- adequacy, reasonable price, reliability -- is linked to OFDI in oil.[2] First, such investment contributes to the adequacy of oil supply by increasing the

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[1] Guy C. K. Leung, "China's energy security: Perception and reality," *Energy Policy*, vol. 39 (March 2011), p. 1332.

[2] Ibid.

flow of oil into the market. Second, supply by national oil companies is deemed to be more reliable than foreign-sourced supplies, especially in the event of crises when state-controlled assets (such as the tanker fleet) can be directed to serve national oil needs. However, national ownership does not protect from natural disasters, political instability in producing countries, terrorist attacks, or military intervention in the Straits of Malacca.[3] Finally, subsidized investment may provide for more stable and predictable prices -- at least if it can be sustained in the long term and thus investment can be protected from market volatility.

Thus, China's investment in foreign oil assets is linked to the country's national energy security objectives. It is not surprising that, in our recent survey of nine state-owned oil companies,[4] government encouragement and resource security were among the top motivations for outward oil investment. But does this investment represent a security threat to other countries?

There are two arguments supporting this concern: first, it is argued that the contest over scarce oil resources may spark confrontation between the US and China; and second, it is argued that China will exert military power to protect its oil assets, by, for example, developing a blue-water navy to shield its tanker fleet or assert its claims on disputed island chains or other territories with strong potential for energy development. Both of these arguments have been frequently challenged.[5] For example, oil produced by Chinese SOEs abroad is sold on the global market and thus benefits all consumers, not only China. Also, China's outward energy investments address a major global energy security concern, namely the lack of investment repeatedly highlighted by the International Energy Agency (IEA).[6] Further, Chinese concerns about the vulnerability of sea lanes and chokepoints are shared by other nations; thus, Chinese efforts to protect them and to diversify trade routes should be welcome.

There are, however, other reasons to be cautious about the rise of China's OFDI in oil. Conventional oil is ultimately a limited resource that produces greenhouse gases. By funding oil exploration and extraction, China is subsidizing greenhouse gas emissions and diverting resources from needed investment in alternative energy technologies. In addition, investment in countries owning oil resources sometimes protects regimes the West considers unsavory.

Investing in oil abroad is not the only Chinese strategy to enhance its energy security. Domestic investments in renewables soared to US$ 50 billion in 2010,[7] as compared to fossil fuel subsidies estimated at US$ 40 billion in 2008[8] and OFDI in oil at US$ 18 billion in 2009.[9] It should also be in China's best interest to see poorly governed oil-rich nations stabilize and more fully integrate into the global trading system. At the same time, the global energy organizations such as the

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[3] ZhongXiang Zhang, "China's energy security, the Malacca dilemma and responses," *Energy Policy*, vol. 39 (December 2011), pp. 7612-7615.

[4] Unpublished survey on Chinese SOEs going global, in collaboration with Euromed, Shanghai; data collected Summer 2011.

[5] Leung, op. cit.

[6] International Energy Agency, *World Energy Outlook 2011* (Paris: OECD/IEA, 2011).

[7] Renewable Energy Policy Network for the 21st century, *Renewables 2011: Global Status Report* (Paris: REN21, 2011), p. 35.

[8] International Energy Agency, *World Energy Outlook 2010* (Paris: OECD/IEA, 2010).

[9] Julie Jiang and Jonathan Sinton, "Overseas investments by Chinese national oil companies: Assessing the drivers and impacts," IEA Information Paper, February 2011.

IEA, largely influenced by European and US interests, should actively involve China in order to ensure more global cooperation and equitable distribution of power.

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