China Papers
No. 19

CIC
Canadian International Council
Conseil International du Canada

ASIA PACIFIC FOUNDATION OF CANADA
FONDATION ASIE PACIFIQUE DU CANADA
25TH ANNIVERSARY
25IÈME ANNIVERSAIRE

The Dragon Returns: Canada in China's Quest for Energy Security

Wenran Jiang

October 2010

Canadian International Council
www.onlinecic.org

Conseil international du Canada
www.cicenligne.org

About the Author

Dr. Wenran Jiang is Mactaggart Research Chair, founding Director of the China Institute (2005-2008) and Associate Professor of Political Science at the University of Alberta. He is a Senior Fellow at the Asia Pacific Foundation of Canada (APF Canada), Special Advisor on China to the Energy Council, Editorial Board member of *Geopolitics of Energy*, a Public Policy Scholar at the Woodrow Wilson International Centre for Scholars in Washington D.C. (September 2009–March 2010) and Project Leader of the Annual Canada-China Energy and Environment Forum (since 2004). Dr. Jiang has written extensively on the rise of China and its impact on the Chinese political economy and the rest of the world, with a major focus on the shifting balance of power in the global economy, international finance and energy and resource sectors. Dr. Jiang is also a *Bloomberg-Businessweek* online columnist, and his op-ed articles and opinions on East Asia and energy issues appear regularly in the Canadian and world media. He is currently completing a book on energy security and Chinese foreign policy.

Acknowledgements

The author would like to thank the CIC and APF Canada for their generous support. Yuen Pau Woo provided much needed guidance as the team leader of this report. Ron Richardson did a great job in editing the manuscript. Thomas Adams provided not only coordination throughout the project but also research and editorial assistance. Simin Yu, Nong Hong and Yu Bao contributed to research and data gathering. The University of Alberta has also provided generous support. And the editorial teams at both the CIC and APF Canada put the report together with their professionalism. I am grateful to all above individuals and organizations while I alone take responsibility for the content and accuracy of this paper.

If you would like to download a copy of this report please visit www.onlinecic.org

If you would like to be added to our mailing list or have questions about our publications please contact: info@onlinecic.org

ISSN 1921-9865 (Online) ISSN 1921-9881 (Print)

Executive Summary

China's continuous economic growth over the past 30 years has created a huge demand for energy and resources, and Beijing's quest for energy security will continue in the coming years and decades. Chinese energy companies have grown into large, integrated and competitive multinational corporations and their "go-out" strategy has left a global footprint of investment, production, joint ventures, supply networks and other forms of presence.

One notable strategy used for large-scale Chinese foreign investment in the energy sector is the "loans-for-energy-supply" accompanied by long-term contracts signed with hosting countries. The recent market downturn has facilitated multi-billion dollar Chinese overseas expansion using this and other models.

There has been a clear correlation between Canada's political relations with China and bilateral energy relations in recent years. Coinciding with the Harper government's lack of engagement with China from early 2006 to early 2009, there was very little Chinese interest in investing in Canada's energy sector; when Ottawa resumed active engagement with Beijing with high-level cabinet visits and summit diplomacy from early 2009, there has been a noticeable jump in Chinese investment in Canada's energy and resource sectors.

With potential large Chinese investment in Canada's energy sector, Canada needs to seek better understanding of China's development and investment dynamics. And in order to effectively engage China, Canada should develop a long-term China strategy in general and in the energy and resource sectors in particular.

Resumé

La croissance économique soutenue de la Chine a créé depuis 30 ans une énorme demande en ressources et en énergie, et cette quête de sécurité énergétique de la part de Pékin se poursuivra au cours des années et décennies à venir. Les sociétés d'énergie chinoises sont devenues de vastes multinationales intégrées et concurrentielles, et leur stratégie « expansive » a laissé une empreinte mondiale combinant investissements, production, alliances et réseaux d'approvisionnement, entre autres manifestations de leur présence.

L'une des principales stratégies chinoises d'investissement étranger à grande échelle consiste à accorder des « prêts en échange d'un approvisionnement énergétique », accompagnés de contrats à long terme signés par les pays hôtes. Et la dernière récession a facilité pour la Chine une expansion étrangère de plusieurs milliards de dollars fondée notamment sur ce modèle.

La période récente a permis d'observer une nette corrélation entre les relations politiques sino-canadiennes et les relations énergétiques bilatérales entre les deux pays. C'est ainsi qu'entre 2006 et 2009, le faible engagement du gouvernement Harper auprès de la Chine a coïncidé avec le très faible intérêt de celle-ci pour tout investissement dans le secteur énergétique canadien. Mais dès qu'Ottawa s'est réengagé activement auprès de Pékin au début 2009 par des visites de représentants ministériels de haut niveau et des rencontres au sommet, on a assisté à un bond notable des investissements chinois dans les secteurs canadiens de l'énergie et des ressources.

Vu le grand potentiel des investissements chinois dans ces secteurs, le Canada doit acquérir une meilleure compréhension de la dynamique chinoise du développement et de l'investissement. Et pour se faire valoir efficacement auprès de la Chine, il doit élaborer à l'égard de ce pays une stratégie à long terme à la fois globale et spécifique aux secteurs de l'énergie et des ressources.

Introduction

China's interests in Canada's energy sector and some of its initial investments were first studied and reported by this author in an APF Canada publication, "Fueling the Dragon, China's Quest for Energy Security and Canada's Opportunities" in 2005.[1] The current study is a follow-up to that report on Canada-China energy relations over the past five years. Canada and China defined energy as one of their most important bilateral policy priorities by signing a joint accord on Canada-China energy cooperation in the 21st century during Prime Minister Paul Martin's visit to Beijing in 2005.[2] Investments in Alberta's oil sands by two large Chinese energy companies, China Petroleum & Chemical Corporation (Sinopec) and China National Offshore Oil Corporation (CNOOC), followed immediately. Soon after, China National Petroleum Corporation (CNPC), China's largest energy firm, signed a $2 billion memorandum of understanding (MOU) with Enbridge for potential cooperation on the Northern Gateway Pipeline project from Alberta to the West coast.

Over the past five years, Canada's energy relations with China have closely followed the pattern of bilateral political relations: cooling off from early 2006 to early 2009, and warming up since early 2009. The public discourse around the Conservative government's amendments to the *Investment Canada Act* based on national security concerns initially had a discouraging impact on potential Chinese investors. This study finds a close correlation between the broader context of bilateral relations and the interests and scale of Chinese investments in Canada's energy and resource sectors. While China's investment, merger and acquisition activities in energy sectors around the world have intensified over the past five years, Chinese energy companies did not invest in large projects in Canada from early 2006 to mid-2009. But they did purchase a significant amount of assets, owned by Canadian firms, elsewhere in the world.

Since the fall of 2009, there has been an identifiable trend, accompanying the resumed summit diplomacy between the two countries, of China showing renewed interest in the Canadian energy and resource sectors. Large investments have begun to come to Canada, and all the large Chinese energy companies are actively seeking potential investment targets, especially in Alberta. There are positive factors contributing to this development, such as the re-affirmed "strategic partnership," a range of good buying opportunities due to the downturn of the market and the stabilized oil prices that are seen as necessary for profitable oil sands exploration. But the Chinese have identified a number of factors still hindering their investment decisions, such as the complex regulatory process for investment and joint venture activities, the high labour cost, the slow expansion of existing and future pipeline capacities from Alberta to the West coast and potential US priorities that may affect the Canadian energy sector.

Meanwhile, Canadian energy companies have experienced a transition from focusing mainly on the United States as their export market to paying more attention to the emerging Asian market, due partly to the financial and economic crises of the past two years, and partly to the realization that diversification may best serve their long-term interests. Yet there are lingering questions as to how to get to know potential Chinese investors better; how to engage in effective negotiations; what is the best level of Chinese investment; and how best to overcome potential physical infrastructure challenges to opening Alberta's vast oil sands to the Chinese and other Asian markets.

This report recommends that Canada conduct a more comprehensive review of the current state of our energy relations with China, identify areas in which Canada has a comparative advantage, organize a more institutionalized consortium of government, private sector and academic cooperation and develop a long-term strategy in working with China in key areas of energy, environment and related sectors.

1 Jiang, *Fueling the Dragon*.
2 People's Republic of China. National Development and Reform Commission. "Statement on Energy Cooperation in the 21st Century."

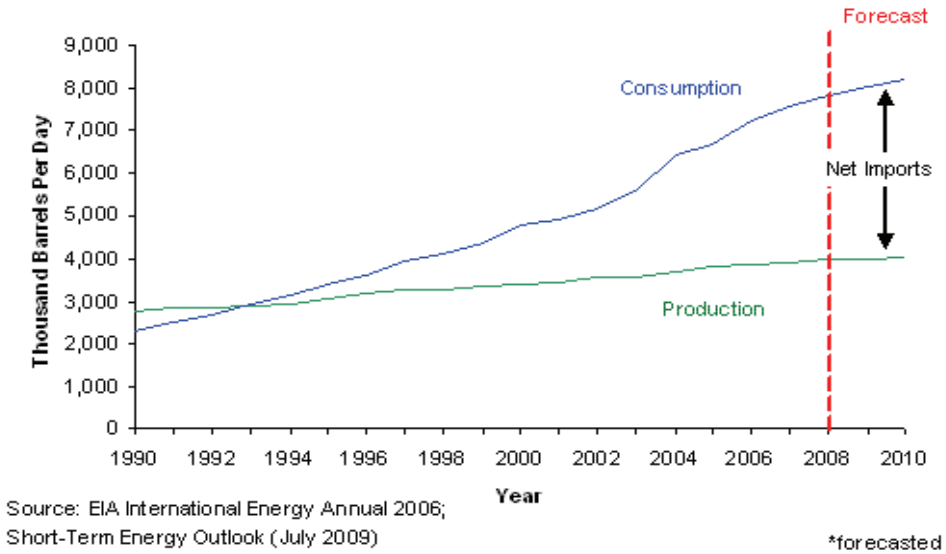
China's Continuous Quest for Energy Security

Economic Growth and Energy Demand

China is now the world's second-largest comprehensive energy producer and consumer after the US. It generates 13 percent of the world's economic output measured by Purchasing Power Parity. China has just overtaken Japan as the second-largest global economy in US dollar terms, and it is poised to surpass Japan as the second-largest energy importer. China is already the world's largest national exporter of goods, largest iron and steel producer and largest automobile producer and market.

The Chinese economy has been growing at over 9 percent annually for the past three decades. The Chinese leadership has pursued a modernization program built largely on traditional economic development models: heavy industrialization, labour- and capital-intensive manufacturing industries, export-led growth, low labour costs and high environmental damage. As part of China's development paradigm, Beijing is following a basic premise laid out by old-school mercantilism on the accumulation of wealth: export as much as possible while discouraging imports where feasible and the larger the trade surplus, the richer and stronger the state. The relatively open international economic system dominated by the US, Japan and other Western powers and the accelerating process of globalization have provided China with a favourable external environment for such a development process. Since joining the World Trade Organization in 2001, China's exports have been rising at an average rate of 29 percent annually.

Figure 1: China's Oil Production and Consumption, 1990-2010*

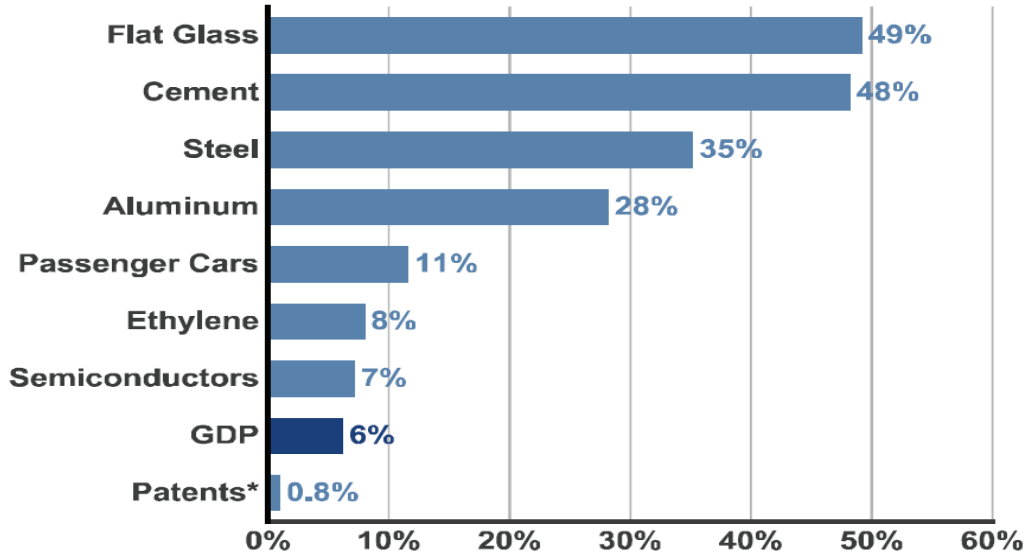


Source: Energy Information Administration. "China - Oil."

But China's "miracle" GDP growth has come with a heavy price tag, including the growing hunger for more and more energy and natural resources, leading to massive extractive activities both inside China and around the world. A fast-growing economy typically requires more energy, but China's modernization drive has produced a manufacturing structure that requires huge increases in energy use, creating an inefficient energy consumption system and a consumer trend that is difficult to sustain. China is now the "factory of the world." The major portion of its economic output is oriented toward industries that are primarily energy-driven. With about

6 percent of global GDP, China consumes 31 percent of the world's coal, 30 percent of iron, 27 percent of steel, nearly 50 percent of cement, 38 percent of copper, 19 percent of aluminum and 10 percent of electricity.[3]

Figure 2: China's GDP and Share of Global Production on Selected Goods, 2006



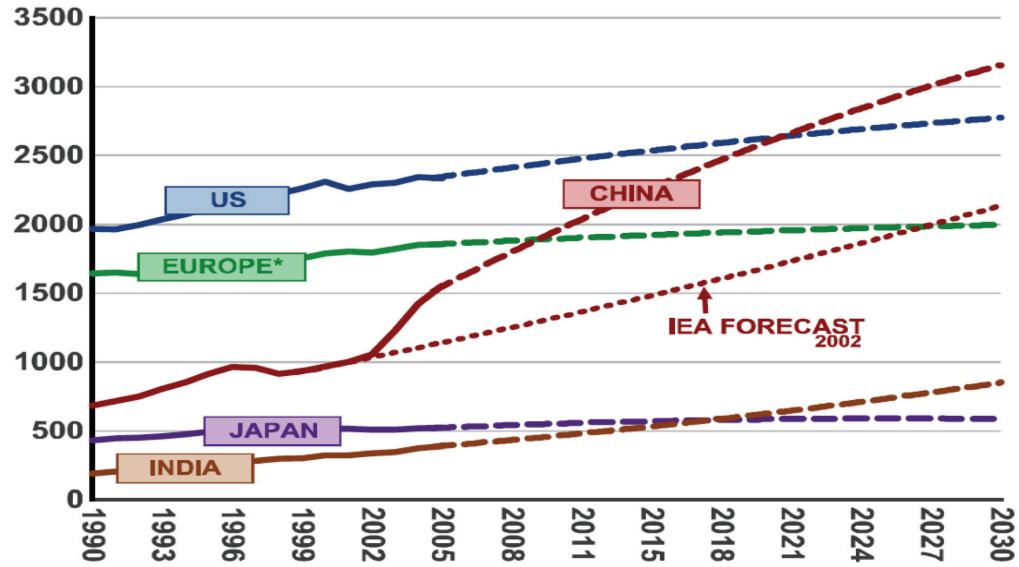
Source: CEIC, USPTO, IEA, Pilkington, IISI, USGS, Comtex, and author's estimates
* Refers to share of US Patents awarded to foreign countries

Source: Rosen, Daniel H., and Trevor Houser. "China Energy: A Guide for the Perplexed." China Balance Sheet. Center for Strategic and International Studies and the Peterson Institute for International Economics. May 2007. Accessed September 27, 2010. http://www.petersoninstitute.org/publications/papers/rosen0507.pdf.

Accompanying this heavy industrial structure is a tremendous waste of energy. As acknowledged by Zhang Guobao, Deputy Commissioner of China's National Development and Reform Commission, to generate every 10,000 *yuan* of GDP (C$1,519), China uses as much as three times the energy as the global average.[4] The ratio is even higher than major advanced industrialized countries. In producing US$1 of GDP, China consumes eight times the energy that Japan does; and in producing the same industrial goods, China uses 11.5 times the energy that Japan does.[5] According to Wang Chao, former minister of China's Ministry of Petroleum Industry, the unit energy consumption level of China's GDP in 2004 was 2.4 times more than the world average; 3.6 times more than the US; 4.9 times more than Germany; 4.4 times more than Japan and 1.6 times more than India.[6] The unit energy consumption of 33 Chinese industrial goods is 46 percent higher than the international average. To generate each tonne of steel, China consumes 40 percent more energy than the international average. Coal supplies nearly 70 percent of China's energy needs. But officially acknowledged statistics show that, in the past 50 years, Chinese coal mines have wasted two tonnes of coal in producing every tonne, resulting in the loss of 65 billion tonnes of coal to produce 35 billion tonnes from 1949-2003.[7]

3 Chen, "Zhongguo Nengyuan Jingzhang Suyuan." Copper consumption rates are based on the first half of 2009, see Holmes, "Global Copper Sales"; Cement consumption rates are for 2009, see High, "Global Cement Demand to Reach 3.5 Billion Tonnes in 2013."
4 Chen, "Fagaiwei: Zhongguo Mei Baiwan Meiyuan GDP Nenghao Shi Riben 9 Bei."
5 "Mei Meiti Cheng Zhongguo Yi Chengwei Shijie Shang Nengyuan Langfei Zui Yanzhong Guojia."
6 Wang. "Wang Tao: Zhongguo De Heping Jueqi Yu Nengyuan Tiaozhan."
7 "Da Youtian Faxian Hou De Yousi: Ziyuan Xingshi Daodi You Duo Yanjun?" ("Troubled Thoughts After Large Oilfield Discovery: Natural Resources Situation Finally Very Grim?")

Figure 3: Energy Demand Forecasts of Major Countries (mtoe)



Source: BP Statistical Yearbook 2006, IEA WEO 2002, IEA WEO 2006. Excludes biomass and waste. *Europe refers to OECD Europe.

Source: Rosen, Daniel H., and Trevor Houser. "China Energy: A Guide for the Perplexed." China Balance Sheet. Center for Strategic and International Studies and the Peterson Institute for International Economics. May 2007. Accessed September 27, 2010. http://www.petersoninstitute.org/publications/papers/rosen0507.pdf.

Yet the country is building one of the most extensive highway infrastructures on earth to replace its one billion bicycles with cars. In 1999, only 220,000 vehicles were sold. In 2004, China produced and sold over five million automobiles, ranking third in the world. By 2009, China's domestic auto production reached 13.79 million units and sales of 13.6 million units, overtaking Japan and the US in both categories.[8] And China's auto industry is projected to grow tenfold between 2005 and 2030.[9] Oil consumed in transportation will account for half of the total oil consumption. Thus China will not only rival the United States in overall national strength in a few decades, but it will also have the largest number of cars – that is if such growth can be sustained.

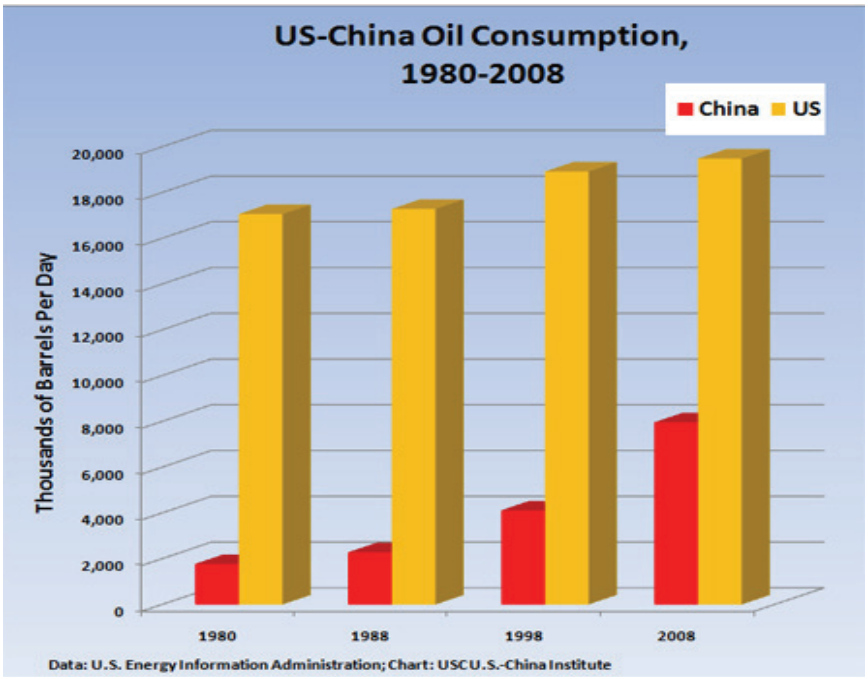
Implications for Energy Policy Formation

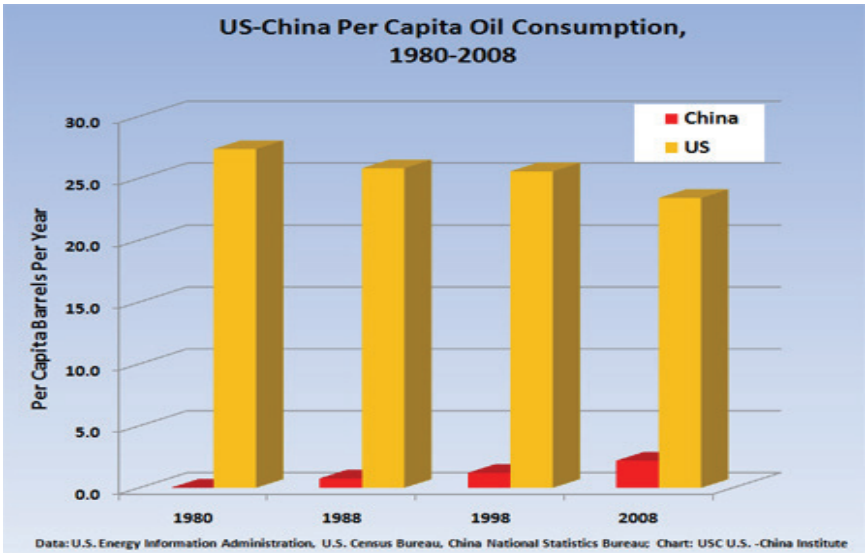
China's relentless pursuit of economic development had turned the country from a petroleum exporter to an importer by 1993, and by the turn of the new century, its dependency on foreign oil had jumped to about 40 percent, and now is at 50 percent. Beijing's new target is to quadruple its economy again between 2000 and 2020, as it did from the late 1970s to the mid-1990s.[10] To achieve that goal, China must rely more and more on external energy supplies. The Middle Kingdom is now burning 8.43 million barrels of oil a day (mbd), a 12.7 percent increase over 2009.[11] Although still far behind the US, which consumed some 20.7 mbd in 2007 and 18.5 mbd in 2009,[12] Chinese consumption is projected to reach a daily level of 10 bpd within the next two decades or so, according to estimates by the International Energy Agency.[13] If every person in China's 1.3 billion population

8 Ren, "China Is Now World Champion in Car Production"; Fang and Subler, "China Tops Global Auto Market in 2009."
9 Watts, "China's E6 Electric Car."
10 Klein, "New Growth Centers in This Globalized Economy," 499.
11 Salaheddin, "China Reaps Benefits of Iraq War with Oil Deals."
12 Energy Information Administration, "Short-Term Energy Outlook."
13 Based on China's average oil consumption rate in 2007, from Flavin, "Oil Price Surge Threatens Economic Stability and National Security."

(today with only 2.4 barrels per person annual consumption) were to have the same per capita consumption as in the US (22 barrels per person per year), China would require more than 80 mbd – about the entire world's current daily consumption.[14]

Figure 4: Energy Consumption – US and China Comparison, 1980-2008





Source: "Economic Crisis, Looming Environmental Threats, and Growing Nuclear Weapons Worries - All in a Day's Work at the Strategic and Economic Dialogue." USC US-China Institute. July 29, 2009. Accessed September 27, 2010. http://china.usc.edu/ShowArticle.aspx?articleID=1557.

14 Mouawad, "China's Growth Shifts the Geopolitics of Oil."

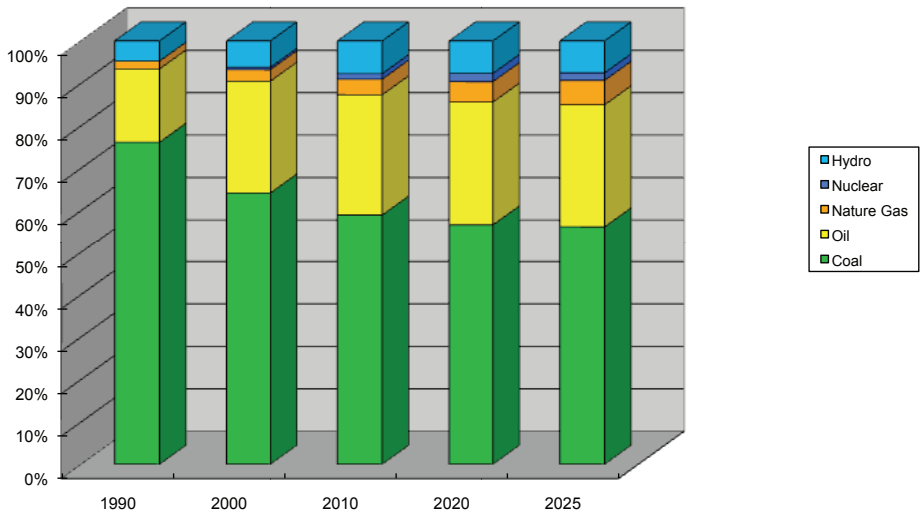
Such a heavy demand for energy and raw materials have led to two major structural imperatives for China. One is to find ever more energy and resources within China's borders and to develop them as quickly as possible to meet the fast growing appetite of major heavy industries and manufacturing capacities. The second is the call by the central government for Chinese enterprises to "go-out," that is, to go around the world to secure, explore and extract additional energy and resources. The high energy and commodity prices prior to the recent world economic recession added urgency to this external push.

The financial and economic crises of the past two years have only heightened the need of such a "go-out" strategy. Zhang Guobao, the head of China's National Energy Administration, described the current energy situation as "opportunities" within "crisis" ("*wei zhong zhi ji*").[15] He identified the symptoms of the crisis as a decreasing demand in the energy sector, such as oil and coal; declining prices of oil, coal and related products; and the deterioration of operating conditions of energy enterprises such as electricity generation, petro-chemical and coal plants. These new developments, as conditioned by the international financial crisis, demanded new thinking and adjustments. Zhang clearly saw more opportunities as he elaborated how China would proceed with a series of new energy policy measures.

First, China's energy strategy must be in concert with the broader $587 billion stimulus package that Beijing has implemented. This means boosting domestic demand and further building up China's energy infrastructure: three new nuclear power plants ($17.5 billion), a second West-East gas pipeline of 5,300 kilometers and related projects ($44 billion), plus a range of other coal, electricity generating and transmission projects.

Second, China must speed up the re-structuring of its energy mix by: expanding large electricity generating plants while reducing the number of small ones; re-organizing coal mining by focusing on 13 large national coal mining areas with large-scale, modernizing operations; increasing the share of electricity generated from nuclear power plants; putting more resources into renewable energy development; and encouraging the development of large energy enterprises.

Figure 5: China's Primary Energy Composition, 1990-2025



Source: Calculations by author from EIA (2004).

15 Zhang, "Dangqian De Nengyuan Xingshi."

Third, China regarded the lower energy and commodity prices during the economic downturn as providing breathing space for the much-needed but complicated on-and-off domestic product oil price reform. Despite the fluctuations in oil prices, the government seemed committed to an "indirect and controlled connection" between domestic and international oil product prices.

Finally, China should take advantage of the lower oil prices not only for importing more oil but also for filling up its strategic petroleum reserves (SPR), a task that was delayed by the persistence of high energy prices in recent years. Zhang indicated that China's first phase of SPR, already in place, had a stockpile capacity of about 100 million barrels of oil, and the second phase now under construction will accommodate 170 million barrels.[16]

In other words, one major structural requirement for China's continuous industrialization drive is to enter energy and resource rich countries to secure supplies. Given Canada's rich endowment of energy, minerals and other key resources, it is only natural that Chinese enterprises see the country as a major frontier to satisfy China's need. And such a need is unlikely to slow down in the foreseeable future. With all the efficiency measures in using energy and the potential of reduced speed in its economic growth, China's demand for traditional energy sources is unlikely to slow down in any substantial way, specifically in the case of demand for oil and gas. This is due primarily to China's energy mix (70 percent coming from coal at the moment). Other than the rapid growth of auto fuels usage, China also wants to replace coal with more oil and gas. The structural demand, therefore, is very strong. China's overall demand for energy will also make it impossible for a substantial slowdown, and this is the prediction of many international energy forecasts.

Chinese Energy Companies Going Global

General Strategies of Engagement

It is an oversimplification to claim that China is so hungry for energy and resources that it will do anything to lock up whatever is available anywhere. China's energy companies have not marched onto the world stage as simple agents of the state. While they receive some guidance from the government, as discussed above, Chinese firms have gone through more trials and experiments of their own in recent years for engaging the outside world. The following set of characteristics is generalized more as behavioural patterns than calculated master plans.

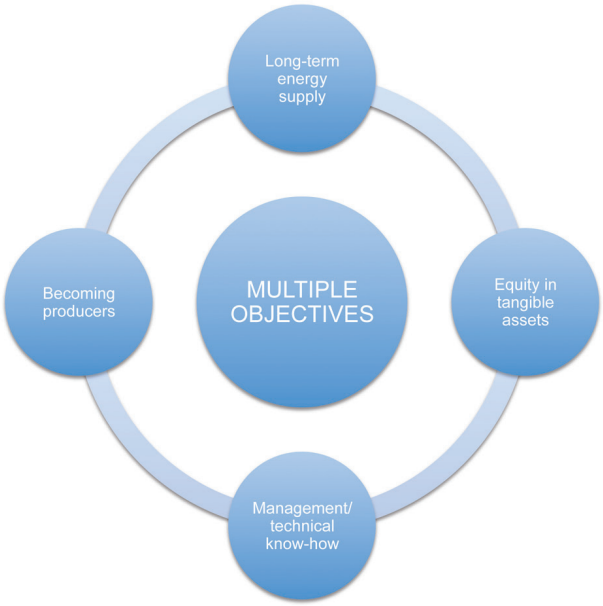
1) **National oil companies (NOCs) are becoming bigger and more integrated globally.** Large Chinese energy companies have begun to diversify from their traditional roles to become bigger, more comprehensive and integrated multinational corporations. In order to cope with competition on the international stage, the top three Chinese energy firms have carried out further reforms in an effort to become more adaptable to a wide range of challenges in foreign environment. CNPC, Sinopec and CNOOC, the three largest NOCs, used to have a clear division of labour. CNPC was designed to be responsible for upstream production in China's major oil fields, mostly located in the northern part of the country. Sinopec focused on downstream refinery and processing activities, which are mostly located in the southern part of China. CNOOC was created to explore offshore oil and gas fields.

   These dividing lines remain but more as areas of professional strength in each company. But the NOCs have also crossed the lines of the historical division of labour, beginning to diversify into others' traditional territories. CNPC now goes downstream while Sinopec goes upstream in their respective corporate expansions. And CNOOC has also moved into on-land production and processing of oil and gas. Such line-crossing activities are most visible in the markets outside

16 "Guoji Youjia Xin Bianshu: Zhongguo 4000 Wan Fang Yuanyou Chubei Tixi Chengxing." ("International Oil Price's New Variable: China's 4 Million Barrel Crude Oil Reserve Is Taking Shape.")

China. According to the *Fortune* 2009 Global 500 ranking for revenues, Sinopec took the 9th place while CNPC occupied the 13th spot. The only other Chinese firm within the top 100 was China Mobil Communications at number 99.[17]

Figure 6: Chinese Energy Companies Going Global: Objectives



Source: Author.

For a list of major global activities by Chinese companies, see **Appendix I: Major Events of China's Energy "Go-Out" Strategy, 2005-2009.**

2) **Building global networks of delivery capacities.** China has focused on building more "Pipelines from the North" and securing "Oil Tankers from the South." Realizing that China's major domestic oil fields have peaked in output, how to manage the fast-growing dependency on imported energy has become a major concern for China. *Bei guan*, or pipeline from the North, characterizes the extensive effort and investment China has put into building transportation infrastructure from Central Asia and Russia. Since 2005, CNPC and the Kazakh oil company KazMunayGas have jointly built the first Kazakhstan-China oil pipeline. With the additional phase to be completed by 2011, the 2,228 kilometer-long pipeline has a capacity of sending 20 million tonnes of oil per year from Central Asia to China. From 2007-2009, CNPC, in joint ventures with Turkmengas, Uzbekneftegas and KazMunayGas, built the first Central Asia-China gas pipeline. Once the second parallel line is completed by the end of 2010, the 1,833 kilometer-long gas line is expected to deliver 40 billon cubic meters of gas per year from Turkmenistan to China.[18] In early 2009, China also signed an agreement with Russia to build a spur to its border from Russia's Eastern Siberia-Pacific Ocean oil pipeline which is under construction, thus winning the competition with Japan for the first destination of Russian oil through this route.

17 "Global 500 2009."
18 For a more comprehensive look at China's pipeline strategy, see Wang, "China-Central Asian Pipeline."

While these arrangements have eased some concern on China's overwhelming dependency on imports from the Middle East and Africa, Beijing remains worried about sea-lane security for some 80 percent of its oil imports via tankers. *Nan chuan*, or Tankers from the South, can be broadly defined as China's efforts in maintaining a smooth flow of sea-lane transportation of energy and resources that are bound for China. While the long-term goal of a blue water navy is being implemented, China dispatched for the first time its destroyers to the Indian Ocean in 2009 to deal with the increasing seizures by Somalia-based pirates. And CNPC also began to build oil and gas pipelines from Burma's deep-water port in the Bay of Bengal to Kunming in China's Yunnan province. This will enable China to diversify the shipping traffic of its imports from the Middle East and Africa via the Strait of Malacca while also shortening the shipping route.

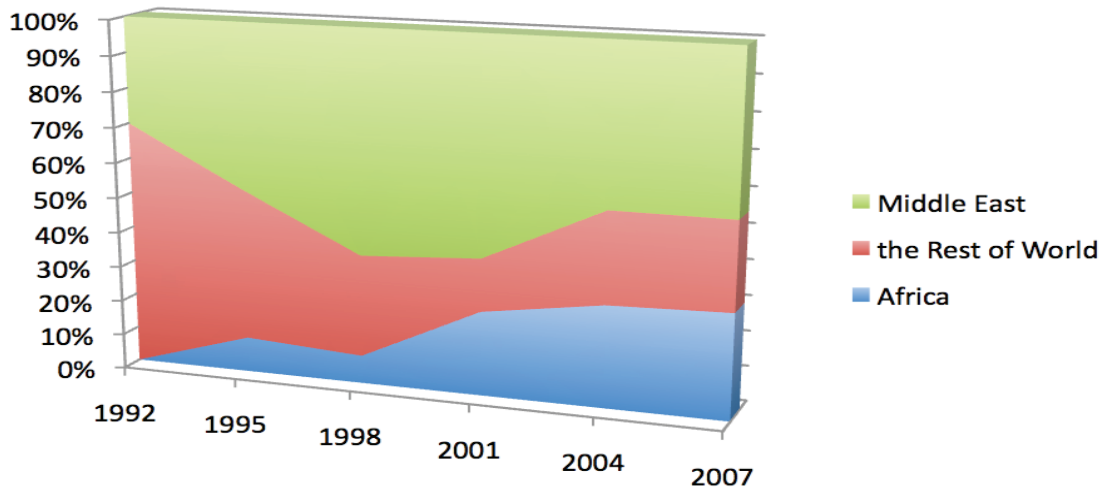
Figure 7: Central Asia/Russia/Myanmar - China Pipelines

Source: Rogers, Michael, and Li Yao. "China's Oil and Gas Balance." PFC Energy. October 2009. Accessed September 27, 2010. http://www.aspo-usa.com/2009presentations/Michael_Rodgers_Oct_13_2009.pdf.

3) **Go wherever the energy resources are.** Chinese energy companies have widespread operations, from Central Asia to the Middle East, from Africa to Latin America. The general increase in trade between China and oil rich countries in recent years has featured substantial energy supplies. Angola is now China's largest African trading partner due to its rapid increase in oil exports to China. Saudi Arabia sold more oil to China than to the United States in 2009.[19] Venezuela, Brazil, Iraq, Sudan and Nigeria all have large Chinese investments in their energy sectors, as does Australia. Though the impact of the failed bid by CNOOC to buy Unocal cast a shadow over Chinese investment in North America, Canada has returned to the list for major Chinese investment in the past year or so.

19 Mouawad.

Figure 8: Sources of China's Crude Oil Imports, 1992-2007



Source: Author.

4) **Bring warm economics together with warm politics and other friendly ties.** The Chinese tend to work with countries that maintain friendly political ties with China. Positive political relations may not necessarily lead to more investment and cooperation by Chinese companies, but the lack of a favourable framework is almost certainly perceived as an obstacle for economic cooperation. China's relations with Middle Eastern countries have been friendly, steady and improving over the decades. Beijing's ties with most African countries are on a firm ground that stretch back to the 1960s. Latin American countries, such as Cuba, Venezuela and Brazil, all have close political and economic relations with China as they collaborate on more energy and resource projects in recent years. The Shanghai Cooperation Organization (SCO) has served as a crucial vehicle in promoting China-Central Asia-Russia relations, and is moving more and more towards the supply of oil and gas to China.

Special Success Formula: Loans-For-Energy-Supply with Long-Term Contracts

General engagement strategies have benefited China's "go-global" drive. But by far the largest Chinese energy investments overseas have all featured a loans-for-energy-supply long-term contract, which involves a mix of state-owned and private actors. For instance, in early 2009, Chinese NOCs struck four major overseas energy deals with Russia, Kazakhstan, Brazil and Venezuela for a combined value of nearly $50 billion in Chinese capital.[20] These complex arrangements indicate that China's expansion into overseas energy assets is a long-term goal and that it is increasingly interested in securing investments from its international partners.

In February 2009, CNPC signed a number of agreements with Moscow, in which China would provide $25 billion in soft loans to Russia in return for a long-term commitment to supply China with oil. In the same month, China and Venezuela agreed to double their joint investment fund to $12 billion by injecting an additional $4 billion from China, in return for Venezuela's state-run oil company PDVSA's commitment to sell CNPC between 80,000-200,000 barrels of oil per day (bpd) by 2015.[21] On February 19, China Development Bank, a financial institution under the State Council primarily responsible for raising funds for large infrastructure projects, sealed

20 Winning, Oster and Wilson, "China, Russians Sign $25 Billion Oil Deal."
21 "China Changing Oil Trade Pattern with Forex Surplus."

a similar deal with Petrobras – the Brazilian state-owned oil major – for a Chinese loan of $10 billion in exchange for a 10-year oil supply memorandum. This agreement will allow China's Sinopec and CNPC to receive up to 150,000 bpd beginning this year, increasing to 200,000 bpd in the next nine years.[22] China's fourth loans-for-oil deal, which was also signed in February 2009, was with Kazakhstan. Under the terms of the contract, Kazakhstan would receive $10 billion in financing for its oil projects. China's Export and Import Bank (Exim Bank), the official export credit agency of the Chinese government, lent the state-owned Development Bank of Kazakhstan $5 billion, while CNPC extended a $5 billion loan to its Kazakh counterpart, KazMunaiGas.[23]

The loans-for-oil deals were unfolding against the backdrop of the global financial crisis, the stock market collapse and abated global oil consumption. Take Russia for example. Rosneft, 75 percent controlled by the government, was burdened with $21.2 billion in debt and Transneft with $7.7 billion.[24] For Rosneft, its $15 billion share of the $25 billion loan from China would comfortably cover its $8.5 billion debt maturing in 2009.[25] China's capital injection complemented the emergency capital needs of national oil firms in Venezuela and Brazil, allowing them to further expand their market shares and turning resources into capital. As for Kazakhstan, China's $10 billion loan could help the Central Asian country initiate its $14.6 billion dollar economic recovery policy.[26]

The global economic crisis has also presented China with a rare opportunity to trade its abundant foreign currency reserves for oil, mineral and other resources around the world. China now has roughly $2.4 trillion in foreign exchange, ranking number one in the world, and many state firms are also flush with funds.[27] Beijing was also considering setting up an oil stabilization fund to support purchases of overseas resources by Chinese oil companies.[28]

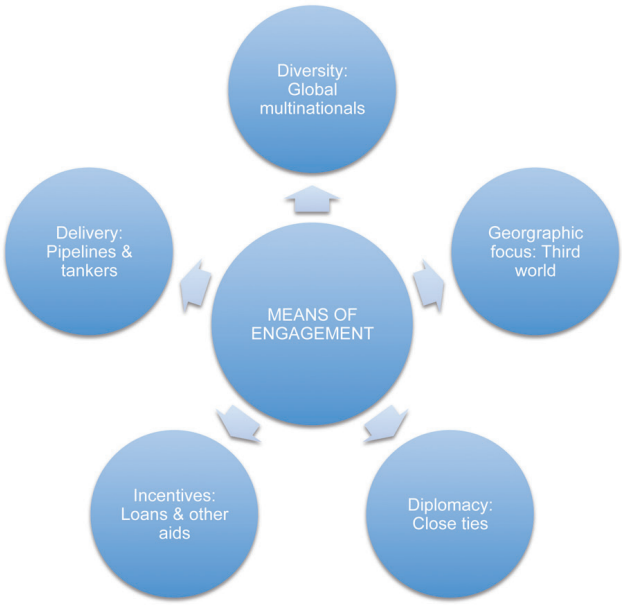
A further facilitating factor for this formula to work was the need for funds and diversification by China's partners. Beijing offered oil-producing nations, especially Russia and Venezuela, an alternative to Western European and US markets, thereby giving them more political clout in the international community and reducing potential vulnerability from their existing buyers. The Russian government plans to increase its crude oil exports to the Asia-Pacific region from 3 percent in 2000 to 30 percent by 2020, amounting to 100 million tonnes a year.[29] Similarly, Venezuela regards China as a key link in its strategy of diversifying oil sales away from the US, which still buys about half of its oil despite years of political tension. The rationale also applies to Kazakhstan. In addition to pipelines extending to Russia and Europe, sustainable oil supplies through the existing China-Kazakhstan oil pipeline can enhance Kazakhstan's energy transit potential by diversify its exporting routes, thereby reducing political and commercial risks.

Yet even under economic pressure, oil-producing countries still kept Chinese oil companies at arms' length during the negotiations. For the former, these four deals represented an optimal outcome – let China provide the financing while they maintain control of the energy assets. The terms of the agreements only gave China the "right to purchase" the oil, but not the "right to own" the oil through equity purchase.

These loans-for-oil activities will remain a component of the Chinese overseas resource acquisition strategy given current global economic and energy conditions. They are accompanied by Chinese NOCs' other commercial and acquisition activities, such as the $8.27 billion offered by Sinopec to buy the Swiss energy company Addax (listed on the Toronto stock exchange) which has large holdings in West Africa and Iraq.[30] The Sinopec-Addax transaction is by far the single largest energy asset purchase by China's NOCs, demonstrating the dynamic nature of China's overseas energy security drive.

22 Fick, "Brazil Petrobras: China Finance Deal Worth $10B Over 10 Yrs."
23 Chen and Chien, "Kazakhstan Expects More Deals with Chinese Firms."
24 Wu and Lin, "After 14 Years of Negotiation."
25 "China/Russia Oil Deal."
26 "Zhongguo Shiyou: 'Daikuan Huan Shiyou' Zaixu, Dingdan Luozi Hazakesitan" ("CNPC: 'Loan-For-Oil' Deal Resumed, This Time Kazakhstan").
27 Kurtenbach, "China Inc. Uses Financial Clout to Lock in Energy, Resource Supplies, Despite Slowdown."
28 "Chinese Oil Firms to Get Financial Support on Forex Surplus for M&A."
29 Itoh, "Russia's Energy Diplomacy toward the Asia-Pacific."
30 "Zhongshihua Shougou Ruishi Shiyou Gongsi Jiaqiang Feizhou Zhanlue."

Figure 9: Chinese Energy Companies Going Global: Engagement Strategies



Source: Author.

Canada in China's Grand Energy Strategy

China's energy and resource needs have been driving its foreign investment in these areas in recent years. A faster-than-expected recovery from the recession in China since 2009, thanks to a US$586 billion government stimulus package in late 2008, has also fueled the demand for more energy and resource supplies. While China has invested tens of billions in countries such as Australia, Brazil, Kazakhstan, Russia and Iran, Chinese investment in Canadian energy assets were largely absent until the fall of 2009. Even during the pre-crisis boom years of the Canadian energy sector from late 2005 to early 2009, Chinese firms made almost no major investment in Canada's energy sector other than CNPC's purchase of over 258.6 square kilometers of oil sands exploration rights in early 2007. During this period, the Chinese purchased energy assets owned by Canadian firms, but almost all of those assets were located outside Canada.

Figure 10: Canadian Firms with Foreign Assets Bought by Chinese NOCs

TIME	COMPANY	PURCHASER	PRICE (US$)	ASSETS LOCATION
Oct. 2005	PetroKazakhstan	CNPC	$4.18 bil.	Kazakhstan
Dec. 2005	Petro-Canada	CNPC & ONGC	$576 mil.	Syria
Feb. 2006	EnCana	Andes Petro CNPC	$1.42 bil.	Ecuador
Oct. 2006	Nations Energy	CITIC Group	$1.9 bil.	Kazakhstan
Jan. 2007	EnCana Chad	CNPC Int'l Chad	$202 mil.	Chad
Dec. 2008	Tanganyika Oil	Sinopec Group	$2 bil.	Syria
Feb. 2009	Verenex Energy	CNPC Int'l	$357 mil.	Libya
Oct. 2009	SouthGobi Energy Resources	China Investment Corp.	$500 mil.	Mongolia

Changing Political Context of Canada-China Relations

In fact, the absence of major Chinese investment coincided with the period when Canada-China political relations were at a very low point. It was just five years ago that China's relations with Canada seemed to be at their peak. On a visit to former Prime Minister Paul Martin in Ottawa in the fall of 2005, President Hu Jintao declared that a bilateral "strategic partnership" – a term that Beijing uses to define key close relations with countries around the world – had been established. The two countries would cooperate in areas ranging from energy security to environment to trade and investment. After the Conservatives ousted the Liberals and formed a minority government in early 2006, however, Sino-Canadian relations entered into a period of uncertainty. In the first three years, Ottawa stopped using the term "strategic partnership" to describe the bilateral relationship. China was removed from Canada's foreign policy priority list. Ideology-based criticism of China from Ottawa intensified. The Harper cabinet suspended all major initiatives for forging closer ties with China previously pursued by the Liberal government, such as Team Canada trade missions and the human rights dialogue. The comprehensive China Strategy, a cabinet level document, was also shelved. And there was little China expertise in the Conservative circle other than that provided by David Emerson, who crossed the floor from the Liberal camp to join the Conservatives.

Harper also decided not to attend the Beijing Olympics in the summer of 2008, an even more explicit message that he was not treating Canada-China relations as a priority. In fact, he did not visit China during his first three years in office, resulting in the suspension of bilateral summit diplomacy. The Conservatives perceived that Canada could carry on a cold relationship with China at the political level while not suffering economically. Another idea floating around at the time was that China needs Canada more than the other way around. There was much discussion about national security threats from Chinese companies, and many perceived the amendment of the Investment Canada Act as a reflection of the worries in Conservative circles that China may come to control Canada's energy and resource sectors. But publicly the Tory government denied that the amendment to the Investment Canada Act was primarily targeting China. Minister of Industry Tony Clement himself also got into controversy by talking about reviews of takeover activities by other foreign firms in Canada.[31]

As a result, Canada lost ground in China on the economic and trade fronts. While trade volumes with China have grown in absolute terms in recent years, Canada's shares of both trade and investment in the world's most dynamic economy have dropped. Despite the overall growth trend, Canada's total trade with China, India and Russia grew only 4.83 percent annually from 2000 to 2009.[32] Investment from the three countries together in Canada in the same period represented only 0.48 percent of Canada's foreign direct investment (FDI) and 0.51 percent of the nation's investment from other countries. In 2009, merely 1.61 percent of China's FDI came to Canada while only 0.33 percent of Canada's FDI went to China.[33] Australia, a country with a much smaller population and economy than Canada, is conducting almost twice as much trade with China as Canada does. While the Harper government underwent a long learning curve in formulating its policy toward China, Beijing displayed no urgency to adopt any fresh initiatives. It took a long time for the Harper Conservatives to realize that the "cold politics, warm economics" formula has been hurting Canada a lot more than China, and the continued disengagement at the highest level would only put Canada in a more disadvantageous position.

Since early 2009, the Government of Canada has changed course in its China policy. Cabinet minister after cabinet minister has been sent to Beijing, reassuring the Chinese that Canada values its relations with China and Chinese investments in Canada are welcome. Ottawa sent consistent, conciliatory messages to Beijing throughout

31 For the newly amended "National Security Review of Investment Regulations" of the Investment Canada Act, see *Canada Gazette Part II* 143, No. 20, 1940-1947. For the related controversies, see Hoffman and McNish, "Clement's Takeover Hangover."

32 According to the recent report by the Standing Senate Committee on Foreign Affairs and International Trade of Canada, over the 2000- 2009 period, 4.21 percent of Canada's total trade, on an average annual basis, was with China; in 2009, trade with China represented 7.01 percent of Canada's total trade. Moreover, imports from China annually averaged 7.03 percent of Canada's total imports over the period; in 2009, 10.86 percent of Canada's imports came from China. Canadian exports to China, on an average annual basis over the 2000-2009 period, were 1.67 percent of Canada's total exports; in 2009, 3.10 percent of Canadian exports went to China. Finally, Canada is China's 11th most important trading partner. See Canada. Standing Senate Committee on Foreign Affairs and International Trade, "A Workplan for Canada in the New Global Economy," 49.

33 Ibid., 50.

the year, culminating in Prime Minister Harper's own visit to China in December 2009. The reasons behind this policy shift are multi-fold: mounting criticism from the business sector, the press and the general public on Harper's neglect of China had made the Conservatives' China policy a liability and potentially a vote-losing factor; Canada's recession generated a more urgent need for accessing the Chinese market; and a much better understanding of China by the formerly inexperienced Conservative foreign policy team.[34]

Policy Recommendation I:

Canada should maintain an overall stable, constructive and friendly relationship with China as specified in the mutually accepted "strategic partnership" concept. Ottawa must continue its regular summit diplomacy with Beijing and further strengthen its political relations with China, which is an indispensible pre-condition for closer economic ties that will benefit both countries.

The Chinese side clearly took notice of such a policy shift in Ottawa, and received Harper warmly. The Chinese media described Harper's trip as an attempt to warm up "cool to icy" ties between Ottawa and Beijing.[35] And the G20 summit in Toronto in June of 2010 provided a good opportunity for Chinese president Hu Jintao to return to Canada, the first Chinese head of state to visit Canada in nearly five years. The Harper government, despite its extremely demanding schedule in preparation for the G20 summit, hosted Hu's formal visit to Canada just two days prior to the G20 gathering in Toronto. The Chinese dispatched by far the largest delegation ever to Canada, with vice premiers, ministers and some 300 senior business executives. In their speeches during the visit, both Harper and Hu expressed optimism over the current state of bilateral relations. Other than signing a range of bilateral agreements for promoting trade, investment and joint ventures, the two countries set a target of reaching $60 billion in bilateral trade by 2015 (currently at $30 billion). And for the first time since the Conservative government came to power in early 2006, Harper used the term "strategic partnership" to describe the nature of the Canada-China relationship, a term that was equally endorsed by Hu.[36] Immediately following Hu's visit, both Canadian Governor General Michaëlle Jean and the Opposition leader Michael Ignatieff visited China, with the latter promising even better relations with China under a Liberal government.[37]

China Returns to the Canadian Energy Sector

> "China's economic engine needs fuel; resources to power and supply its factories; food to feed its workers. Canada has an abundance of natural and agricultural resources to share with China. Our Asia-Pacific Gateway will, in the years to come, be the fastest way to ship goods between North America and Asia." – Prime Minister Stephen Harper

As revealed by multiple Chinese sources, the Harper government's policy shift and the subsequent improvement of the relationship at the political level were important precursors to China's renewed investment activities in Canada's energy and resources sectors. China's well-endowed sovereign wealth funds and other companies have also picked up the pace in investing in Canada's energy, mining and resource sectors in recent months. The recent US$4.65 billion investment by Sinopec in Syncrude Canada Ltd. represents a major renewal of interest in the Canadian energy market by large Chinese oil companies. Sinopec's purchase of ConocoPhillips Co.'s 9 percent stake in Syncrude Group is by far the largest Chinese ownership stake in an active, oil-producing venture in Alberta's energy sector.

34 For more on the shift in the Harper government's China policy, see Jiang, "Canada Needs to Articulate a Clear China Strategy."
35 "Ties with Canada 'to Thaw'."
36 Speeches made by Stephen Harper and Hu Jintao at the Canada-China Business Council gala dinner, June 24, 2010.
37 Schiller, "Michael Ignatieff Gets Warm Reception from Chinese Students."

The Sinopec-Syncrude deal followed closely the $1.9 billion successful purchase by PetroChina (a subsidiary of CNPC) of 60 percent of Athabasca Oil Sands Corporation's MacKay and Dover oil sands projects in late 2009. And in May 2010, the China Investment Corporation (CIC) injected $1.25 billion into Penn West Energy Trust. China has also been actively investing in Canada's mining sectors since 2009 – notably the $1.7 billion equity investment by the CIC in Teck Resources, and the announcement of a $1 billion MOU to forge a strategic alliance between China's State Grid International Development (SGID) and Quadra Mining Ltd.[38]

Three Recent Chinese Investments in Alberta Oil Sands

Joint Venture
PetroChina-Athabasca Oil Sands Corp.

Announcement date:	August 31, 2009
Ministerial approval:	December 29, 2009
Completion date:	February 11, 2010
Investment by PetroChina:	C$1.9 billion
Chinese holding in project:	60-percent stake in two oil sands fields
Potential project scale:	300,000 acres of land and 5 billion barrels of bitumen
Potential future investment:	C$15-20 billion
Related projects:	New refinery that can process 20 million tonnes of heavy oil
AOSC Initial Public Offering:	Completed on April 8, 2010, raising C$1.32 billion

Share Purchase
Sinopec-ConocoPhilips-Syncrude

Announcement date:	April 12, 2010
Ministerial approval:	June 25, 2010
Completion date:	June 27, 2010
Investment by Sinopec:	C$4.65 billion
Chinese holding in project:	9.03-percent stake in Syncrude Canada Ltd.
Potential project scale:	Access to Syncrude's potential 5.1 billion barrels reserve
Related projects:	Consolidation of Sinopec's presence in Alberta

Joint Venture
China Investment Corporation-Penn West Energy Trust

Announcement date:	August 31, 2009
Ministerial approval:	December 29, 2009
Completion date:	February 11, 2010
Investment by CIC:	C$1.25 billion (C$817 million plus C$435 million in trust units)
Chinese holding in project:	45-percent stake in the partnership
Potential project scale:	96,000 hectares of bitumen assets in Northern Alberta

38 As of June 2009, the MOU between SGID and Quadra Mining (now QuadraFNX Mining Ltd.) was no longer effective, and the negotiations continue.

As the following Table shows, relatively large-scale Chinese investment in Canada's energy and mineral sectors have picked up pace since the summer of 2009, coinciding with the warming-up of bilateral political relations.

Major Chinese Investments in Canada since 2009

Date	Company	Purchaser & Joint Venture Partner	Price (US$)
July 2009	Teck Resources	China Investment Corp.	$1.5 billion
August 2009	Athabasca Oil Sands Corp.	PetroChina	$1.7 billion
March 2010	Quadra Mining MOU	State Grid	$1 billion
May 2010	Syncrude	Sinopec	$4.65 billion
May 2010	Penn West Energy Trust	China Investment Corp.	$1.23 billion

As discussed earlier, global oil prices represent another reason why Chinese interest in Canadian energy has grown of late. After a brief nosedive to lows in the US$40 per barrel range during the economic crisis, oil prices climbed back quickly and stabilized in the US$70-$80 range. Various forecasts place the price of oil in coming years at US$80-100 per barrel, a level that can sustain profitability for the extraction of Alberta's oil sands. Over the years, a major question Chinese oil companies have asked during the annual Canada-China Energy and Environment Forum is whether the global market is able to support an oil price range high enough to justify long-term investment in the oil sands. Current oil prices seem to have removed initial doubts, and Sinopec's generous payment for ConocoPhillips' shares in Syncrude displayed a considerable new confidence on the Chinese side.

Annual Canada-China Energy and Environment Forum, 2004-2009

The annual Canada-China Energy and Environment Forum was first launched in 2004 as a major initiative of the China Strategic Working Group of the Department of Foreign Affairs and International Trade (DFAIT). In the 2004 and 2005 annual gatherings, DFAIT provided primary financial support through its Research and Conference Funds. But since 2006, the annual event has been mostly funded by the Canadian private sector and the Canadian academic institutions involved, as well as the two embassies from both countries. Key organizational partners have included the University of Alberta, China Petroleum University, Peking University, Canadian Energy Research Institute, APF Canada and the Canada-China Business Council.

Over the years, the annual event, also called Canada-China Energy Cooperation Conference (2004-2007), has established itself as the most comprehensive mechanism in studying, discussing and debating bilateral energy relations. The annual meeting brings together a large group of private sector participants, government officials and academics from China, Canada, the United States and other countries to address key issues of energy policy, market trends, challenges of cooperation, investment environment, trade barriers and related issues. The forum is not only a platform for policy coordination and academic research, but also an effective vehicle for networking, seeking potential business partners and exploring new opportunities of cooperation. Since 2004, many conference participants have benefited from the annual gathering through direct investment and joint venture opportunities.

2004 Conference in Edmonton: The inaugural conference had only limited Chinese participation and was designed to make an initial assessment of Canada-China energy relations and to take the first steps in cooperation with China in the energy and related sectors. The conference findings and recommendations contributed to the policy formation process that led to the *Canada-China Joint Statement on Energy Cooperation in the 21st Century* during Prime Minister Paul Martin's visit to Beijing in January 2005.

2005 Conference in Beijing: The first ever large-scale bilateral energy conference at Peking University's Centre for Economic Research. A number of Director-Generals from China's National Development and Reform Commission (NDRC) and the State Council spoke to approximately 120 participants from both countries. Representatives from major energy companies made presentations. It was the first time that China registered Canada as a major energy supplier with huge potential, and the conference served to create a positive environment for project cooperation. Not long after the conference, Sinopec and CNOOC made their respective investment in two Alberta oil sands project, Northern Lights and MEG. Enbridge Pipeline Inc. signed a $2 billion MOU with PetroChina for Gateway pipeline cooperation.

2006 Conference in Beijing: The first conference after the Conservatives came to power in Canada. Amid political uncertainties and a clear signal that bilateral political relations were about to cool, the enthusiasm of the private sector from both countries continued to carry the momentum. The meeting addressed key issues such as the market movement, investment climate and the possibility of cooperation on labour. High-tech energy firms such as Westport Innovations Inc. from Canada and the Energy Research Institute of China's NDRC made presentations that opened up further cooperation potential in environmentally friendly technologies.

2007 Conference in Edmonton: The first large-scale bilateral energy relations meeting in Canada. With the strong backing of the Alberta provincial government and the City of Edmonton, China dispatched by far the largest official delegation from its energy sector, including the Director-General of the National Energy Bureau of the NDRC, high ranking officials from CNPC, Sinopec, CNOOC and other big energy firms, China's Ambassador to Canada and embassy officials from the Ministry of Commerce (MOFCOM) and the Ministry of Science and Technology (MOST). In his speech to the conference, Mr. Zhang Xin, Director-General of CNPC's Foreign Affairs Department, announced for the first time that CNPC had acquired 258.6 square kilometers of oil sands exploration rights in Northern Alberta early in the year, with a potential of producing 220,000 barrels of oil if developed in the future. The Chinese energy companies also expressed continued interest in the Canadian energy sector despite the fact that there were political constraints in the bilateral relationship. US Energy Council Chairman, Senator Henry (Hank) Coe of Wyoming, also participated in the conference on behalf of the Council's Executive Committee.

2008 Conference in Beijing: The meeting was held amid the global financial and economic crisis, the plunge in oil prices and uncertainties about the future of oil sands development. Jointly organized with the Canada-China Business Council, the conference was part of a larger event that hosted five Canadian provincial premiers and business delegates from many parts of Canada. The strong display of provincial commitment to improving relations with China put the Harper Conservative government in the spotlight for its lack of engagement with China. More than 100 participants discussed a range of issues on how to

respond to the economic downturn. Featured speakers included the Hon. Shawn Graham, the Premier of New Brunswick; Mei Ping, former Chinese Ambassador to Canada; Xu Dingping, Senior Advisor of the National Energy Leading Group of the State Council; Gao Zhikai, former Senior Vice President of the CNOOC Ltd.; and a number of Director-Generals from NDRC, MOFCOM and MOST.

2009 Conference in Calgary: The first annual meeting to be held in the "energy corporate headquarters" of Canada. The new format of a smaller group of 45 people enabled more in-depth discussion on a range of issues, ranging from the improvement in bilateral political relations to the recovery of the market to China's renewed interest in the Canadian energy and resource sectors. The Canadian Petroleum Producers Association took part in the conference, displaying the newly developed interest by Canadian energy producers to explore potential Chinese investment and possible joint ventures. As predicted by the findings of the workshop, three major Chinese investments, totaling nearly C$8 billion, have occurred between the fall of 2009 to the spring of 2010, marking a new leap forward in Canada-China energy cooperation.

China's renewed interest in investing in Canada has also been helped by the backing of China's state banks in the form of loans and overseas expansion credits to the large state-owned energy and resource companies. Many cash-strapped Canadian energy and resource firms welcome such financial strength and secure funding. At the same time, the North American stock market was hit hard during the economic crisis, and many energy and resources companies have become very good buys – opportunities that do not go unnoticed by the Chinese. So even though the market has recovered significantly, the Chinese are optimistic that the timing is still good, and their investments will yield further returns when the world economy finally climbs out of recession.

Impact of Market Uncertainties

On the other hand, what is less clear is how Chinese energy companies will re-adjust their acquisition activities in Canada and elsewhere given the fact that the global economic recovery is still not stable and many uncertainties lay ahead. Like their Western counterparts, Chinese energy companies were caught off guard by the sharp decrease in oil prices in late 2008.

The dilemma facing both Chinese energy policy makers and large Chinese oil companies was exemplified by Sinopec's purchase of Tanganyika Oil, a Canadian company with its main assets in Syrian oil blocks, in the fall of 2008.[39] When Sinopec, through its wholly owned Mirror Lake Oil and Gas Co. Ltd., offered RMB$2.5 billion (US$2.1 billion) to acquire Tanganyika Oil in September 2008, the price of oil was hovering around US$90 per barrel. But by December, the price had dropped to about US$40. Yet there was no revision of the deal and both China's State Council and the National Development and Reform Commission went ahead with the required government approval.[40]

Many in China saw such a commitment, especially in the face of large financial losses, as a move for the sake of credibility. Others, one of which being the chairman of China's State-owned Assets Supervision and Administration commission, questioned the wisdom of putting so much money abroad without immediate benefits when there was so much need for cash in dealing with the domestic economic downturn.[41] Yet others, represented

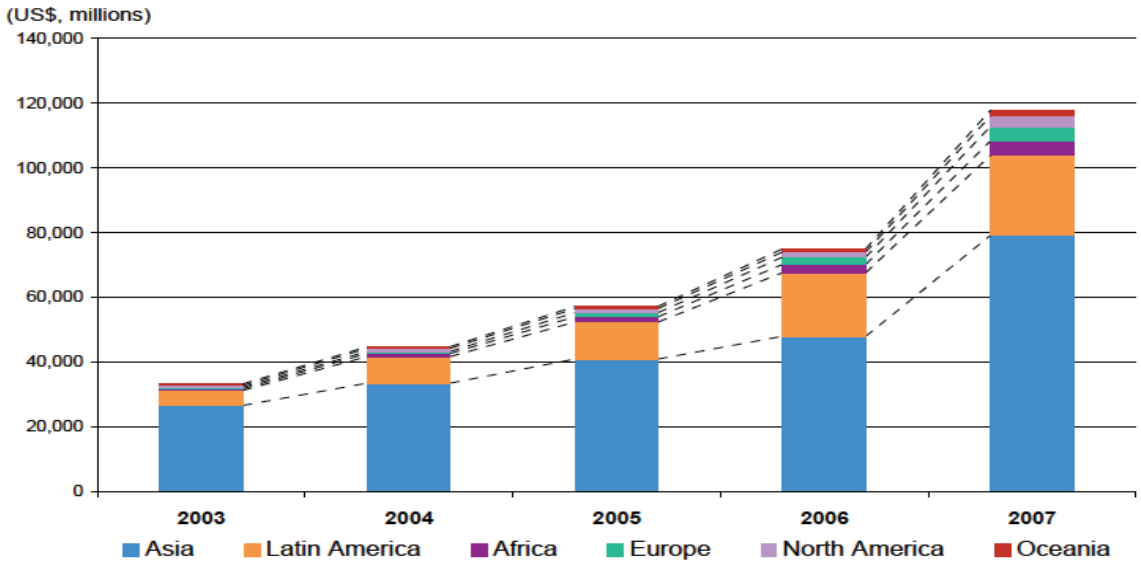
39 "Sinopec Buys Out Canadian Oil Company."
40 "Sinopec to Acquire Tanganyika Oil Company."
41 "Zhongshihua Dui Tanganyika Baiyi Yuan Shougou Huo Pi." ("Sinopec Purchases Tanganyika for 10 Billion Yuan.")

by the China Petroleum and Chemical Industry Association, viewed the purchase as a healthy long-term investment in the expectation that the price of oil would go back up again in the near future. The latter camp seems to have the upper hand.

PetroChina's investment in Athabasca Oil Sands Co. (AOSC) late last year generated much enthusiasm and when AOSC went public, the share price offering was at $18. But due to the recent market fluctuations, the shares of the joint venture have come down to around $10. Whether such a development will have a negative impact on future Chinese investment in Alberta's energy sector is unknown.

But what is obvious is the fact that China's energy policymaking process is far from monolithic. Chinese officials, business leaders and their foreign counterparts are all exploring the implications of China's "go-out" strategy in a time of economic crisis and oil price uncertainty.[42]

Figure 11: Geographical Distribution of China's OFDI Stock, 2003–2007



Source: Korniyenko, Yevgeniya, and Toshiaki Sakatsume. "Chinese Investment in the Transition Countries." European Bank for Reconstruction and Development. Working Paper 107 (January 2009). Accessed September 27, 2010. http://www.ebrd.com/downloads/research/economics/workingpapers/wp0107.pdf.

Policy Recommendation II:

Given China's rapid rise, its continuous growing demand for more energy and resources and its global expansion in these sectors, Canada must prepare itself with a much better understanding of the internal dynamics of China's development as well as the nature, the process and major characteristics of that country's overseas investment strategies.

42 Based on the author's observations as the organizer of the 4th Canada-China Energy and Environment Forum in Beijing in November 2008, and the author's surveys of Chinese press, interviews with Chinese officials and business leaders in the past few months.

A Canadian Strategy for Dancing with the Dragon

The Need for a China Strategy

A close reading of the *Canada-China Joint Statement* released during Prime Minister Harper's visit to China in December 2009 reveals that the Harper government was backpedaling on Canada's commitment to the nature of the bilateral relationship. The joint statement noted that the two sides would resume the "Strategic Working Group" initiative as a bilateral relations enhancement mechanism. According to the agreement, "Deputy Minister-level officials from both sides will meet early in 2010 to discuss the nature of this enhancement and likely subjects of focus, including trade and investment, energy and environment, health and governance." However, the recent visit of President Hu Jintao to Canada served to re-affirm the "strategic partnership" that was announced in 2005.[43]

This development demonstrated that Harper is likely to pursue a forward-looking China strategy. First, slowly and gradually, the Harper government has come to accept that China is Canada's second largest trading partner, and that China has deep pockets in terms of investment. China is also on its way to replacing Canada as the largest trading partner of the United States in the near future. Canada's China challenge is not bilateral and across the Pacific, but right here in North America. Second, Harper's inner circle appears to be moving away from treating human rights and trade promotion as mutually exclusive goals when it comes to China. If Harper proposes a sincere human rights dialogue with China on an equal basis, identifying the right mechanism to implement important human rights programs, Beijing may respond positively. At the same time, Ottawa may pursue economic relations with more vigour and give them serious attention at the highest level of the government.

On the political front, Richard Fadden, the head of the Canadian Security Intelligence Service, made explicit comments to the media that pointed to China as one of the foreign powers trying to influence Canadian politicians. Fadden made it clear that he was warning the public about the dangers posed by foreign governments to Canada's national interests, in an interview with CBC released just two days prior to Chinese President Hu Jintao's visit to Ottawa on June 23-24, 2010.[44] Although Fadden retracted most of his remarks and contradicted himself the day after his interview,[45] he nevertheless insisted again that his accusations were reasonable when he was called to appear before the Parliamentary committee for public safety.[46] The assumption by Canada's spy agency chief that China is Canada's enemy and that pursuing closer relations with China by Canadians of Chinese origin may harm Canada's national interests has given a heavy dose of McCarthyism to the vast majority of Chinese Canadians and many of those Canadian government officials who have worked hard to promote bilateral relations.

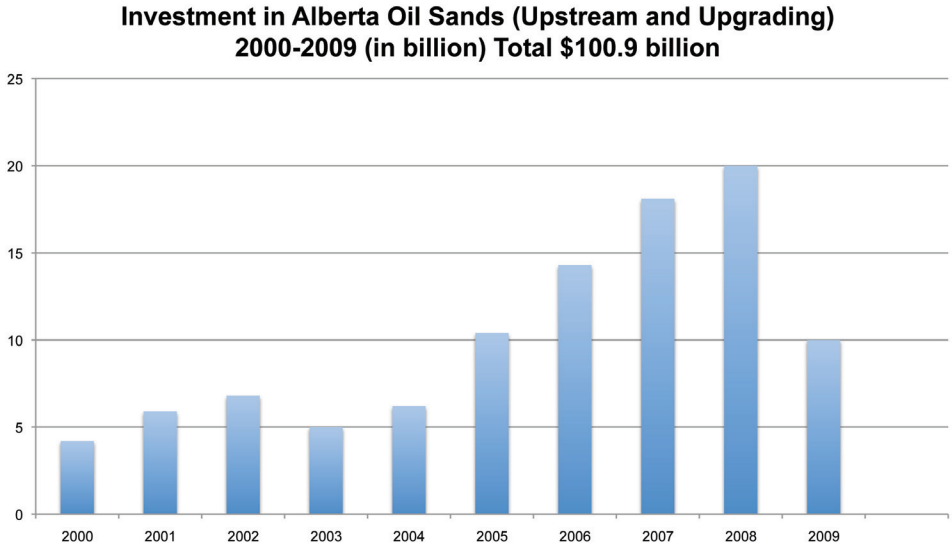
On the economic front, since the Sinopec-Syncrude deal announcement, there has been much talk in Canada about potential Chinese leverage over Alberta's oil sands. While some have repeated oft-heard charges that Chinese investment will lead to Chinese control of Canada's energy and resources – an accusation that lacks credible evidence or research backing – others tend to deliver warning signs that any Chinese voice in the development of Alberta's oil sands may not be conducive to Canada's national interests.[47]

If the smooth approval of the PetroChina-AOSC deal at the end of 2009 and the speedy approval of the Sinopec-Syncrude deal in June of 2010 are any indication, future Chinese investment of this kind should not face substantial questioning or barriers. Tony Clement, the Canadian Minister of Industry, approved the PetroChina-AOSC deal with unusual praise, calling the transaction good for creating jobs, and a "net benefit to

43 Canada. Prime Minister of Canada."Canada-China Joint Statement" and "Canada and China Broaden Strategic Partnership."
44 "Some Politicians Under Foreign Sway: CSIS."
45 O'Malley, "Updated Yet Again with Fadden Statement."
46 "CSIS Boss Defends 'Foreign Interference' Comments."
47 See, for example, McCarthy and Pitts, "Oil Sands Deal Gives China Crucial Veto on Exports," and McCarthey, "Ottawa Puts up Barrier to Sinopec Bitumen Exports."

Canada."[48] The Sinopec purchase of ConocoPhillips' stake in Syncrude represents only 9 percent of the group's overall assets, and its grounds for approval seemed be no different than those of the PetroChina-AOSC transaction.

Figure 12: Total Investment in Alberta Oil Sands, 2000-2009



Source: Author's calculations based on multiple data sources.

Although Sinopec's US$4.6 billion investment is more than twice as big as PetroChina's, the amount is relatively small if measured against either of these companies' overall global investments. The Chinese oil majors have, for instance, involved themselves in large-scale joint ventures in Iraq and Australia.

Thus, the critics have been asking the wrong questions. Not only are Chinese investments in Canada's energy sector small, they are also insignificant in terms of creating leverage to force Canadian shipments of oil to China. Currently, there is no large-capacity, direct pipeline from Alberta to the West coast. Kinder Morgan completed its TMX Loop project in 2008, linking pipelines from Alberta to its existing Mountain pipeline, with a shipping capacity of 300,000 bpd. Even if construction of Enbridge's Gateway pipeline goes ahead as planned, it will not be in place until some time in the middle of this decade, if not later. And as business journalist Deborah Yedlin points out, there is really no need for paranoia: Sinopec's 9.03 percent stake in Syncrude works out to an implied entitlement to about 32,550 bpd, or 11.9 million barrels a year. This amounts to a mere 0.4 percent of China's daily demand for oil. And this number can only fill about 6.2 percent of Enbridge's proposed 525,000-bpd capacity Gateway pipeline.[49]

Policy Recommendation III:

The Canadian private sector, different levels of government, academia and the media should engage in a constructive discourse on the impact of potential large-scale Chinese investment in Canada's energy and resource sectors, and do a better job at informing the Canadian public on the pros and cons of a more robust Canada-China economic relationship.

48 Canada. Industry Canada, "Industry Minister Clement Approves the PetroChina-Athabasca Oil Sands Corporation Transaction."
49 Yedlin, "Paranoia Greeting Sinopec's Oilsands Arrival." Calgary Herald, April 17, 2010.

Canada's Engagement Strategies

If the Canadian business community, different levels of governments, the media and the public in general are to be engaged in a broader discussion of the implications of Chinese investment in Canada, they must be informed by a set of issues associated with potential Chinese investment on a much larger scale.

First, does China insist on shipping its overseas oil production back home? This is clearly not the case for Sinopec's deal with Syncrude. There is no known clause in the transaction that states certain portions of production will be shipped to China. In fact, Sinopec may have made the investment on two assumptions. One is that exporting oil to China will be possible only on a small scale for the foreseeable future, given the existing, modest pipeline infrastructure; the potential for large-scale supply exists only if Enbridge's Gateway pipeline receives the regulatory approval required for construction. Another assumption may well represent a shift in Chinese thinking – that is, they are now willing to invest in Canada's energy sector even without large-scale access to Canadian oil production for China's domestic use. In fact, much of China's global oil production does not wind up being shipped to China. Most Chinese overseas production is sold on the world market as does oil produced by Western oil companies. For the moment, Syncrude's production will continue to flow south to the United States, and Sinopec's 9 percent ownership will not change this arrangement.

Second, is a pipeline that moves oil from Alberta to the West coast, and thus a key component for the ability to ship oil to China, other Asian countries and the US West Coast, still desirable for the Chinese and Canadians? The Chinese have inquired into the state of the Gateway pipeline project in recent years and continue to express strong interest. Their calculus might be understandable: a potential pipeline in place will certainly increase China's incentives for further investing in Alberta's oil sands. This is understandable: although most of China's overseas oil production is sold on the world market rather than shipped home, it is always good to have access to these production sites. The Chinese calculus in Alberta's pipelines to the West coast is not a short-term concern but one of medium to long-term thinking. For Canada, a pipeline or two to diversify international markets will certainly be a benefit, although none of the planned diversification so far will change the fundamental fact that Canada is overwhelmingly dependent on the US market. But it is almost certain that if there are more means of transporting Alberta oil to the West coast, Chinese and other Asian investment interest will increase.

Third, is it in Canada's interests if Chinese and other Asian investors build refineries in Alberta? Currently, most of Alberta's pipelines head south, shipping bitumen to US refineries for value-added upgrading. It has long been accepted on both sides of the border that this is the nature of a North American integrated market. But it is also true that the Alberta government has promoted a development strategy that would see investment to build refineries around Edmonton, thus taking advantage of the booming energy market in creating value-added jobs and products in Canada. If Chinese and other Asian economies become involved in Alberta oil sands extraction, there is good reason to believe investing in refineries is also a part of the long-term strategy, especially under the conditions that upgraded oil products could one day be shipped via increased pipeline and rail capacities to the West coast, and then on to waiting tankers. The recent announcement by the Chairman of PetroChina, Jiang Jiemin, that the company would build a heavy oil refinery in Canada with an annual production capacity of 20 million tonnes of heavy oil is a welcome signal not only for job creation in Canada but also for the long-term diversification of Canada's export markets which, in turn, will produce more value-added jobs and products in Canada.[50]

Fourth, should Canada allow for greater Chinese investment as a part of its diversification strategy from the US market, and if yes, should Canada be worried about a potential US-China competition for Canadian oil? The question begs a response as much from Canada as from China and the United States. For Canada, the answer seems to be more of a market-oriented one than a strategic one. When US demand was booming, there was very little discussion of diversification among Canadian producers. Alberta was happy to ship most of its exports to the south. But the recent economic downturn in the US and the talk of labeling oil sands production as "dirty oil" have alerted Canadians and renewed interest in market diversification. Chinese investment came at this

50 "PetroChina to Build 20-MIn-Ton Heavy Oil Refinery in Canada."

particular time, investment that is welcomed by Canadian producers. There are also indications that both the United States and China are moving in the direction of treating each other as joint venture partners rather than competitors, thus putting Canada in a position of ease rather than angst.

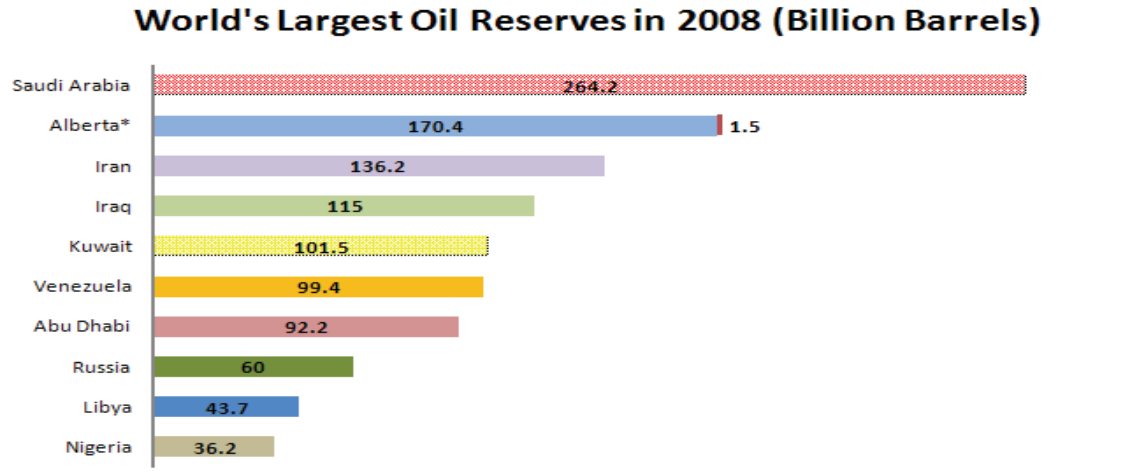
Finally, where is the red line for Chinese investment in Canada's energy sector? How big should it be? Within the global context, Chinese oil companies certainly possess the financial wherewithal to invest, and have done so on a large scale – $10 billion, $20 billion and upward to $40 billion – in other countries. If Canadians are starting to worry over Sinopec's $4.65 billion capital injection, then the nation is not yet ready for any larger investment. The fact is that Canada has all the necessary regulatory frameworks in place to cope with large-scale Chinese investment, and there is no evidence that multi-billion dollar investments by the Chinese in other countries have led to any erosion of host nation sovereignty. The Canadian national discourse needs to focus on whether investment from China will provide social and economic benefits for Canada rather than on parochial debates concerning foreign threats to the resource base.

Policy Recommendation IV:

Canada should conduct a comprehensive review of the current state of its energy relations with China, identify areas in which Canada has a comparative advantage, organize a more institutionalized consortium of government, private sector and academic players and develop a long-term strategy in working with China in key areas of energy, environment and related sectors.

At the level of the Federal government, there is still no particular interest in an Ottawa-driven approach to engaging China – other than making it explicit that Chinese investment is welcome as long as it meets Canadian regulatory requirements. With the Sinopec-Syncrude transaction approved without undo rancor, both Chinese and Canadian energy sectors should be more encouraged and we will likely see other investment or joint venture deals in the near future.

Figure 13: World's Largest Oil Reserves, 2008



*Alberta's total oil reserves were 171.8 billion barrels, of which crude bitumen reserves accounted for 170.4 billion barrels and conventional crude oil reserves for 1.5 billion barrels (note: totals do not add up due to rounding)

Sources: ERCB 2009 ST-98 Report "Alberta's Energy Reserves 2008 and Supply/Demand Outlook 2009 - 2018" and Oil & Gas Journal "Worldwide Look at Reserves and Production. Special Report", December 22, 2008, Vol. 106, Issue 48

Source: Government of Alberta. Energy. "Facts and Statistics." Accessed September 27, 2010. http://www.energy.alberta.ca/OilSands/791.asp.

Canada holds vast oil reserves that could supply China's energy needs for decades to come if the market and transportation conditions are ripe. Currently, Canada's major energy export market is the United States. The pipeline capacities for moving oil to the Pacific coast are also limited. Thus, Canada's stable and potentially increased output benefits China's energy security indirectly as a contribution to the total global output. But if US demand slows down in the future, the China market is a clear alternative. While the current Chinese investments in Alberta's oil sands are not conditional to shipping the output back to China, Chinese oil companies have always expressed a preference that pipelines from Alberta to the Pacific coast, such as the Gateway project, be built. Canada is one of the most stable oil producers, with clear rules and regulations. And as an OECD member, it has a very good investment environment. But it is also important to point out that labour costs are high in Canada, oil sands extraction is expensive and the regulatory approval process is lengthy and complicated. There are also other energy-rich countries that compete for Chinese capital, sometimes with much more favourable terms. If the Chinese are arriving here with wallets at the ready and a desire to do business, Canada needs to think through how much it needs this new investment and how to respond with effective strategies.

Bibliography

Canada. Government of Canada. "Investment Act Canada: National Security Review of Investments Regulation." *Canada Gazette Part II* 143, No. 20 (September 30, 2009): 1940-1947. Accessed September 17, 2010. http://www.gazette.gc.ca/rp-pr/p2/2009/2009-09-30/pdf/g2-14320.pdf.

Canada. Industry Canada. "Industry Minister Clement Approves the PetroChina-Athabasca Oil Sands Corporation Transaction." December 29, 2009. Accessed September 17, 2010. http://www.ic.gc.ca/eic/site/ic1.nsf/eng/05227.html.

Canada. Prime Minister of Canada. "Canada-China Joint Statement." December 3, 2009. Accessed September 17, 2010. http://pm.gc.ca/eng/media.asp?id=3005.

_____. "Canada and China Broaden Strategic Partnership." June 24, 2010. Accessed September 17, 2010. http://pm.gc.ca/eng/media.asp?category=1&id=3476.

Canada. Standing Senate Committee on Foreign Affairs and International Trade. "A Workplan for Canada in the New Global Economy: Responding to the Rise of Russia, India and China." June 2010. Accessed September 17, 2010. http://www.parl.gc.ca/40/3/parlbus/commbus/senate/com-e/fore-e/rep-e/rep07jun10-e.pdf.

Chen, Dai. "Fagaiwei: Zhongguo Mei Baiwan Meiyuan GDP Nenghao Shi Riben 9 Bei." ("NDRC: China's Energy Intensity Per Unit (Million USD) GDP is 9 Times That of Japan.") *Diyi Caijing Ribao*, September 28, 2005. Accessed September 17, 2010. http://news.xinhuanet.com/fortune/2005-09/27/content_3549976.htm.

Chen, Eadie, and Kirby Chien. "Kazakhstan Expects More Deals with Chinese Firms." *Reuters*, April 17, 2009.

Chen, Ya'nan. "Zhongguo Nengyuan Jingzhang Suyuan: 50 Nian Langfei 6 Ge Baiyi Dun Meitian Ziyuan." ("The Origin of China's Energy Supply Crisis: 60 Billion Tonnes of Coal Wasted During the Past 50 Years.") *Zhongguo Shichang*, June 7, 2005. Accessed September 17, 2010. http://finance.sina.com.cn/g/20050607/14461664360.shtml.

"China Changing Oil Trade Pattern with Forex Surplus." *Asia Pulse*, 11 March 2009.

"China/Russia Oil Deal." *The Financial Times*, February 18, 2009.

"Chinese Oil Firms to Get Financial Support on Forex Surplus for M&A." *Xinhua News Agency*, March 2, 2009.

"CSIS Boss Defends 'Foreign Interference' Comments." *CBC News*, July 5, 2010. Accessed September 17, 2010. http://www.cbc.ca/canada/story/2010/07/05/csis-fadden-committee.html .

"Da Youtian Faxian Hou De Yousi: Ziyuan Xingshi Daodi You Duo Yanjun?" ("Troubled Thoughts After Large Oilfield Discovery: Natural Resources Situation Finally Very Grim?") *Xinhua*, May 14, 2007. Accessed September 22, 2010. http://news.xinhuanet.com/politics/2007-05/14/content_6093077.htm.

Energy Information Administration. "Short-Term Energy Outlook." Accessed December 28, 2008. http://www.eia.doe.gov/steo.

Fang, Yan, and Jason Subler. "China Tops Global Auto Market In 2009, Challenges Ahead." *Reuters*, January 11, 2010. Accessed September 17, 2010. http://www.reuters.com/article/idUSTRE60A12220100111.

Fick, Jeff. "Brazil Petrobras: China Finance Deal Worth $10B Over 10 Yrs." *Dow Jones Chinese Financial Wire*, May 19, 2009.

Flavin, Christopher. "State of the World 2005 Global Security Brief #1: Oil Price Surge Threatens Economic Stability and National Security." World Watch Institute. December1, 2004. Accessed September 17, 2010. http://www.worldwatch.org/node/75.

"Global 500 2009." http://money.cnn.com/magazines/fortune/global500/2009/full_list/.

"Guoji Youjia Xin Bianshu: Zhongguo 4000 Wan Fang Yuanyou Chubei Tixi Chengxing." ("International Oil Price's New Variable: China's 4 Million Barrel Crude Oil Reserve Is Taking Shape.") *158*, January 8, 2009. Accessed September 22, 2010. http://www.zf158.com/detail.php?aid=275.

High, Richard. "Global Cement Demand to Reach 3.5 Billion Tonnes in 2013." *International Construction*, February 3, 2010. Accessed September 17, 2010. http://www.khl.com/magazines/internationalconstruction/detail/item51139/Global-cement-demand-to-reach-3-5-billion-tonnes-in-2013/.

Hoffman, Andy, and Jacquie McNish. "Clement's Takeover Hangover." *The Globe and Mail*, July 21, 2009. Accessed September 17, 2010. http://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/clements-takeover-hangover/article1226390/.

Holmes, Frank. "Global Copper Sales – Impact of Chinese Demand." *Mineweb*, July 15, 2009. Accessed September 17, 2010. http://www.mineweb.com/mineweb/view/mineweb/en page36?oid=86253&sn=Detail.

Itoh, Shoichi. "Russia's Energy Diplomacy toward the Asia-Pacific: Is Moscow's Ambition Dashed?" In *Energy and Environment in Slavic Eurasia: Toward the Establishment of the Network of Enviromental Studies in the Pan-Okhotsk Region*, edited by Tabata Shinichiro, 33-64. 21st Century COE Program Slavic Eurasian Studies, No. 19 (2008). Accessed September 17, 2010. http://src-h.slav.hokudai.ac.jp/coe21/publish/no19_ses/2_ito.pdf.

Jiang, Wenran. "Canada Needs to Articulate a Clear China Strategy." Canadian International Council. The Foreign Exchange (December 2, 2009). Accessed September 17, 2010. http://www.onlinecic.org/blogs/ciccommentary/canadaneedstoarticulateaclearchinastrategy.

_____. "China and India Come to Latin America for Energy." In Energy Cooperation in the Western Hemisphere, edited by Sydney Weintraub. Center for Security and International Studies. 2007.

_____. "China's Economic Growth and Its Global Quest for Energy Security." In China, India and the United States: Competition for Energy Resources. The Emirates Centre for Strategic Studies and Research, 2008.

_____. "China's Emerging Strategic Partnership in Africa." China Into Africa: Trade, Aid, and Influence, edited by Robert I. Rotberg. Washington, DC: Brookings Institution Press, 2008.

_____. "China's Global Quest for Energy Security." Canadian Foreign Policy 13, No. 2 (2006): 105-131.

_____. "Chinese Industry and Foreign Policy: Lessons for Canada." Canadian International Council. China Papers (July 2010). Accessed October 7, 2010. http://www.onlinecic.org/download/resourcece/archives/chinapapers/cic_chinapapersno14_jiangpdf?attachment=1.

_____. "Fueling the Dragon: China's Quest for Energy Security and Canada's Opportunities." Asia Pacific Foundation of Canada. Canada in Asia (April 2005). Accessed September 17, 2010. http://www.asiapacific.ca/sites/default/files/archived_pdf/can_in_asia/cia_fueling_dragon.pdf.

_____. "Fueling the Dragon: China's Rise and Its Energy and Resources Extraction in Africa." The China Quarterly 199 (September 2009): 585-609.

Jansson, Johanna, Christopher Burke, and Wenran Jiang. "Chinese Companies in the Extractive Industries of Gabon & the DRC: Perceptions of Transparency." The Centre for Chinese Studies, University of Stellenbosch. January 2009. Accessed October 7, 2010. http://www.ccs.org.za/wp-content/uploads/2009/11/Chinese_Companies_in_the_Extractive_Industries_of_G abon_and_the_DRC._CCS_report_August_2009.pdf.

Klein, Lawrence R. "New Growth Centers in This Globalized Economy." *Journal of Policy Modeling* 26, Issue 4 (2004): 499-505.

Kurtenbach, Elaine. "China Inc. Uses Financial Clout to Lock in Energy, Resource Supplies, Despite Slowdown." *The Associated Press*, February 18, 2009.

McCarthy, Shawn. "Ottawa Puts up Barrier to Sinopec Bitumen Exports." *The Globe and Mail*, April 14, 2010. Accessed September 17, 2010. http://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/ottawa-puts-up-barrier-to-sinopec-bitumen-exports/article1534790/.

McCarthy, Shawn, and Gordon Pitts. "Oil Sands Deal Gives China Crucial Veto on Exports." *The Globe and Mail*, April 13, 2010. Accessed September 17, 2010. http://www.theglobeandmail.com/report-on-business/industry-news/energy-and-resources/oil-sands-deal-gives-china-crucial-veto-on-exports/article1533681/.

"Mei Meiti Cheng Zhongguo Yi Chengwei Shijie Shang Nengyuan Langfei Zui Yanzhong Guojia." ("American Media: China's Energy Waste the Worst in the World.") *Zhongguo Shiyou Wang*, August 11, 2005. Accessed September 17, 2010. http://finance.sina.com.cn/chanjing/b/20050811/15411879877.shtml.

Mouawad, Jad. "China's Growth Shifts the Geopolitics of Oil. " *The New York Times*, March 19, 2010. Accessed September 17, 2010. http://www.nytimes.com/2010/03/20/business/energy-environment/20saudi.html?_r=1&partner=rssnyt&emc=rss.

O'Malley, Kady. "Updated Yet Again with Fadden Statement – Shorter PMO on CSIS/Fadden Allegations: Heck If We Know." *CBC News*, June 23, 2010. Accessed September 17, 2010. http://www.cbc.ca/politics/insidepolitics/2010/06/shorter-pmo-on-csisfadden-allegations-heck-if-we-know.html.

People's Republic of China. National Development and Reform Commission. "Statement on Energy Cooperation in the 21st Century." January 24, 2005. Accessed September 17, 2010. http://en.ndrc.gov.cn/newsrelease/t20050620_8220.htm.

"PetroChina to Build 20-Mln-Ton Heavy Oil Refinery in Canada." May 21, 2010. Accessed September 17, 2010. http://news.alibaba.com/article/detail/business-in-china/100308458-1-petrochina-build-20-mln-ton-heavy-oil.html.

Ren, Jie. "China Is Now World Champion in Car Production." *China Daily*, February 3, 2010. Accessed September 17, 2010. http://www.chinadaily.net/bizchina/2010-02/03/content_9420521.htm.

Salaheddin, Sinan. "China Reaps Benefits of Iraq War with Oil Deals." *Associated Press*, June 9, 2010. Accessed September 17, 2010. http://www.washingtontimes.com/news/2010/jun/9/china-reaps-benefits-of-war-with-oil-deals/.

Schiller, Bill. "Michael Ignatieff Gets Warm Reception from Chinese Students." *Toronto Star*, July 5, 2010. Accessed September 17, 2010. http://www.thestar.com/news/world/article/832234--ignatieff-gets-warm-reception-from-chinese-students.

"Sinopec Buys Out Canadian Oil Company." *China Daily*, December 26, 2008.

"Sinopec to Acquire Tanganyika Oil Company." *Oil Voice*, September 25, 2008. Accessed September 22, 2010. http://www.oilvoice.com/n/Sinopec_to_Acquire_Tanganyika_Oil_Company/0c87f255.aspx.

"Some Politicians Under Foreign Sway: CSIS." *CBC News*, June 23, 2010. Accessed September 17, 2010. http://www.cbc.ca/canada/story/2010/06/22/spying-csis.html.

"Ties with Canada 'to Thaw'." *People's Daily Online*, December 2, 2009. Accessed September 22, 2010. http://english.peopledaily.com.cn/90001/90776/90883/6829539.html.

Wang, Tao. "Wang Tao: Zhongguo De Heping Jueqi Yu Nengyuan Tiaozhan" ("Wang Tao: China's Peaceful Rising and Its Energy Challenge.") *Renmin Ribao*, April 9, 2004. Accessed September 17, 2010. http://scitech.people.com.cn/GB/25509/37822/40305/3360642.html.

Wang, Zhen. "China-Central Asian Pipeline: Implications for China's Energy Security." *Geopolitics of Energy* (August-September 2008).

Watts, Jonathan. "China's E6 Electric Car: 'We're Not Trying to Save the World – We're Trying to Make Money'." *BusinessGreen*, April 3, 2009. Accessed September 17, 2010. http://www.businessgreen.com/business-green/news/2239795/china-e6-electric-car-trying.

Winning, David, Shai Oster, and Alex Wilson. "China, Russians Sign $25 Billion Oil Deal." *Dow Jones*, February 17, 2009.

Wu, Qiong, and Lin Jiangyang. "After 14 Years of Negotiation, Russian Oil Pipeline Runs into China." *Xinhua News Agency*, May 19, 2009.

Yedlin, Deborah. "Paranoia Greeting Sinopec's Oilsands Arrival." *Calgary Herald*, April 17, 2010. Accessed September 17, 2010. http://siliconinvestor.advfn.com/readmsg.aspx?msgid=26472250.

Zhang, Guobao. "Guojia Nengyuan Juzhang Zhuanwen: Dangqian De Nengyuan Xingshi "Wei" Zhong Zhi "Ji"." ("National Energy Administration Director Writes: The Current Energy Situation "Opportunity" within "Crisis"") *Renmin Ribao*, December 29, 2008. Accessed September 17, 2010. http://news.xinhuanet.com/fortune/2008-12/29/content_10572847.htm.

"Zhongguo Shiyou: 'Daikuan Huan Shiyou' Zaixu, Dingdan Luozi Hazakesitan" ("CNPC: 'Loan-For-Oil' Deal Resumed, This Time Kazakhstan.") *Xinhua News Agency*, April 19, 2009.

"Zhongshihua Dui Tanganyika Baiyi Yuan Shougou Huo Pi." ("Sinopec Purchases Tanganyika for 10 Billion Yuan.") *Caijing*, December 15, 2008. Accessed September 22, 2010. http://www.caijing.com.cn/2008-12-15/110039181.html.

"Zhongshihua Shougou Ruishi Shiyou Gongsi Jiaqiang Feizhou Zhanlue." ("Sinopec Purchases Swiss Oil Company, Strengthens Africa Strategy.") *SZOnline*, June 25, 2009. Accessed September 17, 2010. http://szonline.net/Channel/content/2009/200906/20090625/168927.html.

Appendix I: Major Events of China's Energy "Go-Out" Strategy, 2005-2009

(For transactions involving Canadian firms, see Appendix II)

April 2005: China and Bangladesh sign an MOU on Oil and Gas Cooperation.

November 2005: A Chinese company is scheduled to undertake three-dimensional seismography in Iran's Changluleh oil field.

December 2005: CNOOC signs a production-sharing agreement with Devon Energy Corp. for deepwater block 42/05 in the South China Sea. CNOOC has the right to participate in up to a 51-percent interest in the event of any commercial discovery in the block.

January 2006: China and Saudi Arabia sign five agreements, including one on greater energy cooperation.

February 2006: CNOOC Africa Ltd., a subsidiary of CNOOC, signs a five-year production-sharing contract with GEPetrol for the offshore Block S in Equatorial Guinea.

April 2006: Chinese President Hu Jintao and Yemeni President Ali Abdullah Saleh sign eight agreements covering energy, economic, trade, telecommunications and other fields.

April 2006: CNOOC signs a production sharing agreement for oil and gas exploration of Kenya's Block L2 in the offshore Lamu Basin.

April 2006: The Chinese government agrees to invest US$4 billion to upgrade Nigeria's 110,000-bpd Kaduna Refining and Petrochemicals Company and build a railroad system and power stations in exchange for CNPC being granted four oil drilling licenses.

April 2006: CNPC purchases exploration rights to the oil and gas Manokwari Block located in Papua Province of Indonesia from PT Waropen Perkasa.

April 2006: Sinopec signs a US$239 million agreement with Brazil's Petrobras to build a 300-kilometer long natural gas pipeline linking northern and southern gas fields in Brazil.

June 2006: CNOOC Ltd. announces that Phase I of Southeast Sumatra (SES) Gas Project has been brought on stream. 55 million cubic feet of gas per day will be delivered via four wells. CNOOC Ltd. owns a 65.5-percent stake in Southeast Sumatra PSC.

June 2006: Sinopec acquires 27.5, 40 and 20-percent stakes, totalling US$692.2 million, for three deep-water oil blocks off Angola through its joint venture with Sonangol E.P. – Sonangol Sinopec International – in which Sinopec owns a 75-percent stake. The three blocks contain proven oil reserves of 3.2 billion barrels.

July 2006: The Chinese government approves a US$5 billion joint venture between Sinopec and Kuwait Petroleum Corp. to build a petrochemical plant in Nansha in Guangdong Province which will produce 1 million metric tonnes of ethylene a year.

August 2006: Sinopec acquires 99.49-percent stake in Udmurtneft from TNK-BP for US$3.5 billion. In its turn, Sinopec Russia's Rosneft will buy 51-percent stake in Udmurtneft and Sinopec will keep the remaining 49 percent.

August 2006: China agrees to invest US$5 billion in new and existing energy projects in Venezuela through 2012 as part of a plan to boost Venezuela's oil output and oil sales to China.

September 2006: Following the 2003 acquisition of a 12.5-percent stake in BP's Indonesian Tangguh LNG project, CNOOC Ltd. finalizes an agreement in which the Tangguh facility will ship 2.6 million tonnes per year of LNG to CNOOC's LNG terminal in Fujian Province starting in 2009 for the next 25 years.

October 2006: The Chinese government approves the establishment of a pipeline from Turkmenistan to Guangzhou for the transport of natural gas. The pipeline will begin to transport 30 billion coalbed methane over 30 years starting in 2009.

December 2006: CNOOC, US ConocoPhillips and UK Premier Oil win oil and gas exploration rights for 18 blocks in Indonesia. The three companies will make a combined investment of US$235 million for the initial three years.

December 2006: CNOOC finalizes an MOU with Iran's NIOC to develop Iran's North Pars gas field. The US$16 billion agreement will last for 25 years.

December 2006: China Oilfield Services Ltd. (COSL) enters agreements with GOIMAR S.A de C.V for construction and provision of services for four module rigs in the Gulf of Mexico. COSL will be responsible for the investment and construction of the module rigs, mobilization, installation and rig-up, with each module rig to be employed for three years.

December 2006: Sichuan Honghua Petroleum Equipment Co., Ltd. signs an agreement with three Egyptian companies to establish an oil drill manufacturing company in Egypt. Both parties will each invest US$15 million.

December 2006: China National Oil and Gas Exploration and Development Corp. (CNODC), a subsidiary of CNPC, reaches an agreement on joint exploration of oil and gas with Uzbekistan's Uzbekneftegaz. CNODC plans to invest more than US$200 million in oil and gas exploration in Uzbekistan over the next five years.

January 2007: CNOOC joins Indonesia's PT SMART and Hong Kong Energy (Holdings) Ltd. to invest US$5.5 billion in producing biofuel in Indonesia.

February 2007: Sinopec signs a contract with Saudi Arabia's Aramco and US Exxon Mobil Corp. on a US$4 billion refinery upgrade. The refinery in Quanzhou in Fujian Province will process primarily Saudi crude supplied by Aramco. Sinopec will own 50 percent of the joint venture, while Aramco and Exxon will each hold a 25-percent stake.

April 2007: CNOOC and Sinochem Corp. prepare separate bids for the West African oil and gas assets of US-based Devon Energy Corp. in a deal valued at between US$1.5 billion and US$2 billion.

December 2007: Sinopec and the National Iranian Oil Company (NIOC) finalize a US$2 billion agreement to develop Iran's Yadavaran oil field. Sinopec owns a 51-percent stake, NIOC owns a 20-percent stake and India's ONGC Videsh owns a 29-percent stake. Phase 1 of the Yadavaran project will produce 85,000 bpd and Phase 2 will produce 185,000 bpd.

January 2008: Sinopec will invest US$5 billion and cooperate with Indonesia's PT Puri Usaha Kencana enterprise to set up biofuel factories in Indonesia.

August 2008: PetroChina and Sinopec make a joint bid of between US$2.5 billion for offshore assets in Peru owned by Petro-Tech Peruana.

December 2008: Chinese companies make numerous loans totalling US$3.2 billion to Indonesian companies for various energy projects.

February 2009: The China Development Bank loans Russia's Rosneft and Transneft US$15 billion and US$10 billion respectively in exchange for 300,000 bpd per year for the next 20 years and the completion of a pipeline from Siberian oilfields to northern China.

March 2009: CNPC begins operation of the Al-Ahdab oilfield in Iraq following the US$3 billion service deal signed the previous year. The oilfield is expected to produce up to 115,000 bpd in six years.

April 2009: CNPC signs two loan agreements with Kazakhstan's KazMunaiGas and the Development Bank of Kazakhstan, totalling $10 billion for financing oil and other projects.

May 2009: The China Development Bank finalizes a loan agreement with Brazil's Petrobras in which it will loan Petrobras US$10 billion. In exchange, Petrobras will supply Sinopec will 150,000 bpd for the first year and 200,000 bpd for the following nine years.

July 2009: CNOOC Ltd. and SIPC (subsidiaries of CNOOC and Sinopec respectively) announce that they have formed a joint venture for the purchase of a 20-percent stake valued at US$1.3 billion in Block 32, an offshore oil asset in Angola, from Marathon International Petroleum Angola Block 32 Ltd., a subsidiary of Marathon Oil Corp.

August 2009: PetroChina, CNPC's publicly listed arm, signs an US$41 billion supply contract with Exxon Mobil Corp. to purchase 2.25 million metric tonnes of LNG per year for 20 years from the Gorgon field in Australia.

August 2009: Sinopec Group buys Geneva-based Addax Petroleum Corp. through its wholly-owned Sinopec International Petroleum Exploration and Production Corp. (SIPC) for US$7.5 billion, the largest overseas takeover transaction yet made by a Chinese oil company. As a result, Sinopec gains control of Addax's oilfields in Iraqi Kurdistan and Nigeria.

September 2009: A consortium led by CNPC and BP wins the joint bid of Iraq's Rumaila oilfield project. CNPC holds a 37-percent stake, BP holds a 38-percent stake while Iraq's South Oil Company holds the rest. The consortium will invest approximately US$15 billion over the contract's 20-year term to increase the oilfield's current output of 1 mbd to approximately 2.85 mbd.

November 2009: Sinopec Corp. signs its first liquefied natural gas (LNG) purchase deal with US oil major Exxon Mobil Corp. Sinopec will purchase 2 million tonnes of LNG per year for 20 years from Exxon Mobil's Papua New Guinea project.

Appendix II: Major Canada-China Transactions in Energy and Resource Sectors, 2005-2010

April 2005: PetroChina and Enbridge Inc. enter into an MOU to cooperate on the development of Enbridge's Northern Gateway pipeline project. The proposed C$2.5 billion pipeline will transport approximately 525,000 bpd from Alberta to the West coast to be shipped to American and Asian markets.

April 2005: CNOOC acquires a 16.69-percent stake for C$150 million in MEG Energy Corp. which owns a 100-percent working interest in over 32,900 acres of oil sands leases, with an estimated 2 billion barrels of recoverable reserves.

June 2005: Sinopec buys Synenco Energy's 40-percent stake in Total E&P Canada's Northern Lights Oil Sands Project for C$105 million. The project is expected to eventually produce more than 100,000 bpd.

September 2005: A CNPC and Sinopec Corp.-led consortium called Andes Petroleum Company reaches an agreement to purchase Canada-based EnCana Corp.'s assets in Ecuador for US$1.42 billion. The consortium acquires five blocks in Ecuador, capable of producing 75,200 bpd with proven reserves of 143 million barrels of oil, as well as a 36-percent stake in OCP Pipeline.

October 2005: CNPC purchases Canada-registered firm PetroKazakhstan for US$4.18 billion. CNPC subsequently cedes 33 percent of its shares to Kazakhstan's KazMunaiGas.

August 2006: CNOOC signs three new product-sharing contracts with Husky Oil China Ltd. for the exploration of deep-water oil blocks in the South China Sea.

December 2006: China's CITIC Group gains a 100-percent stake in Nations Energy Co. Ltd. when it buys its Karazhanbas oil and gas field in Kazakhstan for US$1.91 billion. The field contains proven reserves of over 340 billion barrels of oil and currently produces over 50,000 bpd, which CITIC Group can develop until 2020.

June 2007: CNPC wins the exploration rights to 11 sections of a 258.6-kilometer oil sands project. The project is said to eventually yield 220,000 bpd. This is the first instance of a direct purchase of a controlling stake made by a Chinese company into the oil sands.

January 2008: Atomic Energy of Canada Ltd. and the Nuclear Power Institute of China sign an MOU for collaborative research and development of nuclear technology that uses less uranium in response to a possible future shortage of the fuel.

April 2008: More than 100 private Chinese oil producers intend to invest a total of US$30 million to establish 40 biodiesel bases in Canada to facilitate fuel exports to China.

June 2008: Husky Energy signs an accord with CNOOC to add exploration Block 63/05 to its acreage in the South China Sea.

December 2008: Sinopec completes the acquisition US$2 billion of Canada-listed Tanganyika Co. which produces heavy oil in Syria. Tanganyika's board of directors is replaced with Sinopec appointees and the company is delisted from the Toronto Stock Exchange.

April 2009: Sinopec buys a 10-percent interest in Total E&P Canada's Northern Lights Oil Sands Project, adding to the 40-percent interest it purchased in the project from Synenco Energy in 2005.

April 2009: CNPC approaches PetroCanada and Suncor Energy to purchase their offshore assets in Libya and Syria valued at US$5 billion.

April 2009: China Gas Holdings Ltd. forms a strategic partnership with IMW Industries Ltd. to develop compressed natural gas for natural gas vehicles in China and around the world. IMW will supply a minimum of 120 compressed natural gas fuelling stations over the next three years.

June 2009: Consolidated Thompson Iron Mines Ltd. signs a deal with China's Wuhan Iron and Steel (Group) Corp. for a US$240 million investment that will help fund the development of the company's Bloom Lake project.

June 2009: CNOOC and PetroChina plan to bid for a 35-percent stake in InterOil's proposed US$4.5 LNG project in Papua New Guinea, worth US$500 million.

July 2009: CIC acquires a 17.2-percent stake in Teck Resource Ltd. for US$1.5 billion. The acquisition of 101.3 million Class B shares provides CIC with a 6.7-percent voting share in the company.

September 2009: CNPC pulls out of the C$499 million agreement it signed in April to purchase Verenex Energy, which includes its 50-percent share of the Area 47 property in Libya, following the Libyan government's refusal to approve the deal.

September 2009: China's largest nickel trader is taking a 15-percent stake in Royal Nickel Corp., a privately held junior miner led by a group of former Inco executives, including ex-chief executive officer Scott Hand.

October 2009: Zijin Mining Group Co. says it agrees to buy 12.8 percent of the enlarged outstanding shares of Canada-listed Continental Minerals Corp. for C$22.6 million.

October 2009: CIC agrees to invest US$500 million in a Mongolia-focused Canadian-listed coal company.

February 2010: CIC has been quietly accumulating stakes in resource firms including Canada's Kinross Gold Corp. and Potash Corp. of Saskatchewan, according to a filing with securities regulators.

February 2010: PetroChina Co. completes a C$1.9 billion acquisition of a 60-percent working interest in Athabasca Oil Sands Corp.'s MacKay River and Dover oil sands projects.

March 2010: The State Grid Corporation of China (SGCC), a state-owned public utility, plans to cooperate with Canadian miner Quadra Mining Ltd. to jointly develop copper mines in Chile, to secure raw material supplies for electric cables and to expand its investment portfolio.

April 2010: Jinchuan Group Ltd., a China-based non-ferrous metallurgical and chemical engineering enterprise, has made an offer to acquire all of the common shares of Crowflight Minerals, Inc., a Canada-based junior mining company, in consideration for an aggregate cash payment of C$150 million.

May 2010: CNPC signs an MOU with the province of Saskatchewan to help the province develop its energy assets.

May 2010: PetroChina Co. Ltd. announces its intention to build a heavy oil refinery in Canada with an annual production rate of 20 million tonnes of oil.

May 2010: CIC signs an agreement with Penn West Energy Trust to form a partnership to develop Penn West's bitumen assets in the Peace River area of Alberta through its wholly-owned subsidiary. CIC will invest C$817 million and will acquire a 45-percent stake in the project while Penn West will invest C$1.8 billion and retain a 55-percent stake. CIC also invests C$435 million for a five-percent equity stake in the trust.

June 2010: Tongling Nonferrous Metals Group Holdings Co. and the China Railway Construction Corp. have jointly acquired a 96.9-percent stake in the Canadian mining company Corriente Resources Inc.

June 2010: The Canadian government approves Sinopec International Petroleum's purchase ConocoPhillips' 9.03-percent stake in Syncrude Oil Sands Project for US$4.65 billion. This is China's second largest investment in North America.

The CIC Canada-China Relations Project

Bilateral relations between the governments of Canada and the People's Republic of China are a matter of strategic interest to Canada. Recent changes in the frequency of high-level visits, the effective style and content of bilateral communications and perspectives held about each country by various sectors of each other's society all suggest that the Canada-China relationship has changed significantly in recent years. Yet China remains vitally important to Canada for a variety of reasons and in a variety of sectors. Political and diplomatic cooperation on issues of direct bilateral concern and also on issues of global import remains critically important. Commercial and trade ties linking Canada with the world's third largest and fastest growing economy are of obvious importance. Cultural and civil society ties, including immigration patterns and the ancillary effects they generate, are also important. In these and other matters, the Canada-China relationship will likely grow in importance in the years to come. While the diversity of links between Canada and China militates in favour of giving due attention to a multiplicity of commercial, academic and civil society links, bilateral cooperation at the federal/central government level remains important.

In keeping with CIC objectives to advance research and dialogue on international affairs issues of importance and interest to Canadians, the CIC Canada-China Relations Project has focused on supporting research and analysis toward building a policy framework for Canada's relationship with China. The project's activities have been developed along three thematic areas that reflect issues of common concern: a) Chinese domestic institutional and normative contexts for engagement; b) Economic relations; c) Collaboration on global issues such as environment, health and security.

a) Domestic Context for Engagement: The Canada-China relationship can be most effective when it is grounded on complementarity of interests, which in turn requires mutual understanding of domestic normative and institutional conditions in both countries. Canadian initiatives with China, ranging from WTO compliance and business regulation to human rights, can be effective only if they are designed and implemented in light of China's domestic conditions, ranging from popular norms to governmental structures and policy priorities. Similarly, China's success in nurturing productive relationships with Canada will require appreciation of Canadian domestic conditions. The papers for this thematic area were commissioned and directed by Professor Jeremy Paltiel of Carleton University.

b) Economic Relations: Economic relations between Canada and China are critically important. Economic relations include bilateral trade and investment relations, and also extend to local effects of economic conditions and behaviour. In the trade area, Canada's strengths match up extremely well with China's needs. In trade and investment relations, efforts to promote normative and institutional accommodation in China for Canadian business objectives are consistent with Chinese development policies and also serve important Canadian interests in the areas of good governance. As well, national economic behavior by the two countries in response to changing economic conditions at the global, regional and local level have important effects on the Canada-China relationship. The papers for this thematic area were commissioned and directed by Yuen Pau Woo, President of the Asia Pacific Foundation of Canada.

c) Collaboration on Global Issues: The importance of China's responsible participation in systems for addressing global policy concerns in areas such as environment, health and security cannot be overstated. Yet China's participation in the global community can be distorted by its responses to apprehension and competition from other global actors, particularly the United States, the European Union and Japan. Canada has a significant role to play in supporting China's responsible participation, not only through direct bilateral programming but also through our capacity to deploy good offices, legitimation and other soft power resources both bilaterally and globally. The papers for this thematic area were commissioned and directed by Professor Brian Job of the University of British Columbia.

The papers here presented in connection with the CIC Canada-China Relations Project offer informed, nonpartisan recommendations for a variety of stakeholders in Canada, including the government and private and public sector institutions and individuals, with a view toward furthering the development of healthy long-term relations between Canada and China. While historical and current conditions may result in disagreement as to how best to manage the Canada-China relationship, China's importance to the world requires our attention. We hope that the papers presented here can further the process of understanding and effective engagement that will strengthen the foundation for productive relations for the long-term interests of both countries.

Dr. Pitman B. Potter

Chair
CIC China Working Group

The Canadian International Council (CIC) is a non-partisan, nationwide council established to strengthen Canada's role in international affairs. With local branches nationwide, the CIC seeks to advance research, discussion and debate on international issues by supporting a Canadian foreign policy network that crosses academic disciplines, policy areas and economic sectors.

The CIC features a privately funded fellowship program and a network of issue-specific Working Groups. The goal of the CIC Working Groups is to identify major issues and challenges in their respective areas of study and to suggest and outline the best possible solutions to Canada's strategic foreign policy position on those issues. The CIC aims to generate rigorous foreign policy research and advice.

CIC Board of Directors

45 Willcocks Street, Box 210
Toronto Ontario M5S 1C7
TEL: 416-977-9000, 1-800-668-2442
FAX: 416-946-7319