

China, Oil and the Risk of Regional Conflict

By Mamdouh G. Salameh*

As China approaches the twenty-first century, the future of its oil industry is causing it mounting trepidation. In 1993, China became a net crude oil importer for the first time.¹ In the face of declining oil reserves, flagging output and rising domestic consumption, China must make significant new oil discoveries if it is to maintain the momentum of its economic growth and avoid becoming heavily dependent on oil imports in the late 1990s and beyond. The Chinese are now struggling, not so much to increase, but just to maintain their current levels of oil production. They have been over-producing to meet their domestic needs at the risk of depleting their reserves and causing serious damage to their oil wells' reservoirs. The Chinese are not finding enough reserves to replenish what they have extracted, thus causing an annual deficit in their oil balance.

In its drive to find new oil reserves, China has been targeting two major oil provinces, the Tarim basin in the northwest of the country and the South China Sea, both of which are believed to contain potentially large oil reserves. Yet to achieve its objectives, China will have to surmount substantial financial and technical obstacles and, in the case of the South China Sea, added geopolitical and strategic problems complicated by territorial claims which could escalate into armed conflict between China and some of its Southeast Asian neighbors, especially Vietnam.

Of course, oil and geopolitics can continue to be a volatile mixture. After all, the first of the post-Cold War crises was the Gulf crisis, which was, in its essence, about oil and geopolitics.

The China Oil Factor

China's spectacular economic growth and its growing thirst for oil will impact most forcefully on the geopolitics of the Asia-Pacific region in the coming decade. And if China's economic growth continues at its current pace, it will become the world's third biggest crude oil importer after the United States and Japan. By the year 2000, China will need to import more than 2 million barrels per day (mbd) of crude oil if no substantial new oil resources are found. This could have a tremendous impact on global oil supplies and the price of oil. It could also have a significant impact on the strategic environment and the balance of power in Southeast Asia in view of China's search for oil reserves in the disputed territories surrounding the Spratly Archipelago in the South China Sea.

One thing, however, is certain. China will be as robust as the United States in defending its access to oil supplies. Furthermore, China may not shy away from the use of force to defend its rights of access. However, to satisfy its oil needs, China may look to the Middle East, Southeast Asia or Siberia. It could trade arms for oil with the Middle East or could use arms to secure oil supplies from Southeast Asia,

* Mamdouh G. Salameh is an international oil economist, a consultant to the World Bank in Washington and a technical expert of the U.N. Industrial Development Organization in Vienna. He is also a member of the International Institute for Strategic Studies in London.

¹ See footnotes at end of text.

especially from the South China Sea.²

China's Oil Fundamentals

China's proven oil reserves at the start of 1995 stood at 24 billion barrels (bb) with a reserve-to-production ratio of 22 years.³ Estimates put China's proven and potential reserves at around 68 bb, of which 39 bb are onshore reserves and 29 bb offshore reserves. These estimates exclude potential reserves in the disputed territories surrounding the Spratly Islands in the South China Sea, estimated by some accounts to range from 7-130 bb.⁴

China became a net crude oil importer for the first time in 1993 and is projected to become increasingly dependent on oil imports between now and the year 2000. And to compound the problem, domestic oil consumption has been rising at an average annual rate of 8 percent between 1990 and 1994 while production has risen by an average rate of 1 percent during the same period (see Table 1).

Table 1
China's Crude Oil Production Vs. Consumption
1990-2000 (mbd)

	1990	1991	1992	1993	1994	1995	2000 ¹	%Chg 90-00
Production	2.79	2.81	2.85	2.90	2.91	2.89	2.47	-11.5
Consumption	2.27	2.41	2.66	2.98	3.00	3.24	4.53	+100
Balance	0.52	0.40	0.19	-0.08	-0.09 ²	-0.35	-2.06	

¹ Forecast figures

² During 1994 China imposed quotas for crude oil and products imports.

Source: BP Statistical Review, 1995; China Energy Study, 1995, East-West Center, Honolulu, Hawaii, USA; Author's Projections.

In 1994, 80 percent of China's oil output originated from fields near the northeast coast, some of which have already peaked. The offshore sector produced 76,824 barrels a day (b/d) accounting for a mere 2.6 percent of total oil output (see Table 2).

Table 2
China Onshore and Offshore Oil Production Forecast
1990-2000 (mbd)

	1990	1991	1992	1993	1994	1995	2000
Total Production	2.79	2.81	2.85	2.90	2.91	2.89	2.47
Offshore Prod.	0.03	0.04	0.05	0.06	0.08	0.08	0.17
As % of Total	0.90	1.30	1.70	2.20	2.60	3.00	7.00

Source: BP; China Energy Study; Author's Projections.

Faced with declining oil reserves and rapidly growing domestic consumption, China is under increasing pressure to find new reserves. Without any new oil finds, oil imports are projected to rise over the remainder of this decade, reaching an estimated 2.06 mbd by 2000 (see Table 3).

Table 3
China's Crude Oil Exports and Imports
1985-2000 (mbd)

	1985	1990	1991	1992	1993	1994	1995	2000
Exports	0.60	0.53	0.40	0.19	-	-	-	-
Imports	-	-	-	-	0.20	0.09 ¹	0.35	2.06

¹ Import quotas were introduced in 1994.

Source: BP; China Energy Study; OPEC Annual Statistical Review.

In its drive to find new oil reserves, China has been targeting the Tarim basin in the northwest corner of the

country and the South China Sea.

The Tarim basin is the largest under-explored oil basin in the world. Here, trapped under the sands of this uncommonly harsh terrain, lie potential reserves estimated at 147 bb or more than six times China's current proven reserves.⁵ That is one reason why Beijing finally allowed foreign oil companies to explore the basin.

In the offshore regions, the area with the greatest potential is the South China Sea.

China's Economic Success and Security Policy

China's influence will grow over the next decade or two as its economic power develops.

Estimates of the size of China's economy vary considerably. The International Monetary Fund (IMF) calculates that, on the basis of purchasing-power parity, China's Gross National Product (GNP) is slightly smaller than Japan's (\$ 4,592 bn) and larger than those of France and the U.K. combined (\$2,469 bn), thus giving it an estimated size of \$2,469 bn to \$4,592.⁶

Some analysts project that by 2005, China's economy will have overtaken Japan's to become the second largest economy in the world after the United States.⁷ There is, however, a general consensus among experts that China can sustain growth rates of 7-10 percent per annum, implying a doubling of its GNP every 7-10 years.⁸

Whatever the precise calculations of China's future economic size relative to the U.S. and Japan, there is no doubt that China's economic power will affect the other Asian nations and will bring about a remarkable shift in the international balance of power. A positive link exists between China's economic success and its security policy. This has been demonstrated in recent years by China's enhanced capability for projecting power in and through the South China Sea in pursuit of its territorial and maritime claims.⁹

But economic success could also act as a constraint on Chinese security policy. Will an economically powerful China risk upsetting its neighbors in Southeast Asia over the South China Sea, when it is trying to attract investment and secure markets? The answer to that question will be determined by the power structure in the post-Deng China and also by China's need for foreign investment and technology. China's thirst for oil means that the development of the oil sector will be given top priority in investment plans. This will entail an estimated investment of more than \$15 bn in the Tarim basin and the South China Sea. However, the size of this investment is so substantial that some observers doubt whether China could muster the necessary resources on its own.¹⁰

A Potential Asian Conflict Ahead?

Oil wealth beneath the South China Sea is fueling an explosive arms race in Southeast Asia. Every nation touching the waters between Japan and the Straits of Malacca has either announced or begun a major weapons build-up, fearing that a post-Cold War withdrawal of U.S. and Russian forces will bring long-suppressed territorial and maritime claims to a boil.

It is China's thirst for oil and its claims of sovereignty over the Spratly islands that is a major concern among the five

other claimants of the islands, namely Taiwan, Vietnam, Malaysia, Brunei and the Philippines. The Spratlys are a valuable strategic prize, not only because they lie among major shipping lanes, but also because they lie atop substantial undersea oil and gas reserves.

In the past few years, Southeast Asian nations have watched with growing alarm as China has gone about developing a potent blue-water force with which to back its territorial claims. None of China's Southeast Asian neighbors can begin to match China as an emerging naval power. They are convinced, too, from all the evidence at hand, that the United States is withdrawing from the region as a geopolitical force and that, they fear, is creating a dangerous vacuum of power, one that China is only eager to fill.

At this stage, no one can say for sure whether China's current attempts to expand its influence reflect aggressive intentions or are simply the natural consequence of rising power.

Still, the threat of conflict is real. China threw down the gauntlet on 25 February 1992 when it passed a law asserting sovereignty over the Spratly, Paracel and Senkaku Islands and other specks in the South China Sea and warned it would defend them. But Japan told Beijing bluntly that the Senkaku Islands are Japanese indigenous territory. Since then, Malaysia, Vietnam and the Philippines have reinforced their troop strength in the Spratly archipelago.¹¹

Consequently, this mix of overlapping territorial disputes, the continued build-up of military forces in close proximity to each other and the history of use of force by China in the recent past against Vietnam, could, in the absence of a settlement, give rise to the threat or use of force.

Conclusions

A settlement between China and the Southeast Asian claimants over the Spratly Islands could move the South China Sea disputes off the geopolitical stage and with them the opportunity for involving foreign outside powers. However, for a real settlement to be stable and equitable, it must be based on multilateral arrangements for the joint development of the potential oil and gas resources in the Spratly archipelago, which satisfy most of the central concerns of the claimant-states. Such arrangements must take into account the interests and the conflicting sovereignty claims as well as the need to acknowledge China's preeminent position as the leading regional power and also accommodate the interests of extra-regional maritime powers such as Japan and the United States.

If Beijing were to throw its weight behind such a solution, it could usher in an era of fruitful economic and prosperous co-operation between the nations of the region. However, despite all hopes of improvement, the most likely scenario for the future of the South China Sea is the status quo. But the status quo may be acceptable as long as relations among the claimants are good, or at least, not hostile. It could, through an unexpected political or military event, be transformed into open conflict.¹²

In the final analysis and in the absence of a real settlement, China will probably prevail either by its willingness to exercise force or the realization by the Southeast Asian nations that they cannot stand against China in the absence of a credible American counterweight. Either way,

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