

# ENERGY SECURITY AND ENERGY DIPLOMACY OF CHINA AND INDIA IN THE 21<sup>st</sup> CENTURY

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The commodity markets of the early 21<sup>st</sup> century were determined by the dramatic rise of demand and prices. It was one of the biggest “super-cycles” in commodity markets in history<sup>1</sup>. This rise was especially notable in the oil market. While in 1998 the price of a barrel of oil was only 12.72 USD, in 2008 it was already 97.26 USD (data for Brent dated<sup>2</sup>). After a brief but considerable fall of prices in the second half of 2008, they rose up in 2009–2010 and stabilized in 2011–2013 on the level of over 100 USD/b<sup>3</sup>. In autumn 2014 they started to fall again<sup>4</sup>. The reason behind this “super-cycle” was the rise of demand from emerging markets, especially China and India<sup>5</sup> on the one hand, and insufficient investment in new production capacities in the 1990s on the other hand<sup>6</sup>. While traditionally in international relations natural resources are associated with conflicts rather than with cooperation<sup>7</sup>, it is not surprising that it is also in the 21<sup>st</sup> century that concerns arose that the competition for scarce resources would emerge and eventually lead to resource wars<sup>8</sup>. Rising oil demand from China and India was the reason behind the growing resource nationalism all over the world<sup>9</sup>. Since the International Energy Agency (IEA) forecast indicates that in the period of 2005–2030 the two

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<sup>1</sup> O. Canuto, *The commodity super cycle: is this time different?*, World Bank Group, Economic premise no. 150. Washington, D.C., 2014.

<sup>2</sup> See: *Dated Brent: Oil Price Assessments*, Platts, [www.platts.com/price-assessments/oil/dated-brent](http://www.platts.com/price-assessments/oil/dated-brent), (accessed on: 28 July 2016).

<sup>3</sup> *BP Statistical Review of World Energy June 2016*, p. 14.

<sup>4</sup> J. Baffes, A. Kose, F.L. Ohnsorge, M. Stocker, *The great plunge in oil prices: causes, consequences, and policy responses*, World Bank Group, Policy Research Note; PRN/15/01, Washington, D.C., 2015; B. Fattouh, *Adjustment in the Oil Market: Structural, Cyclical or Both?*, The Oxford Institute for Energy Studies, Oxford Energy Comment 2016.

<sup>5</sup> J. Baffes, *The role of emerging-market economy demand during the post-2005 boom*, World Bank, Washington, DC 2012.

<sup>6</sup> Policy Development and Review Department, *Oil Market Developments and Issues*, IMF, 2005, p. 10.

<sup>7</sup> A. H. Westing (ed.), *Global Resources and International Conflict: Environmental Factors in Strategic Policy and Action*, Oxford, Oxford University Press, 1986; T. F. Homer-Dixon, *Environment, Scarcity, and Violence*, New Jersey, Princeton University Press, 1999.

<sup>8</sup> M. Klare, *Resource Wars: The New Landscape of Global Conflict*, New York, Henry Holt and Company, 2001.

<sup>9</sup> V. Vivoda, *Resource nationalism, bargaining and international oil companies: challenges and change in the new millennium*, in „New Political Economy”, vol. 14, no. 4, 2009, pp. 517-534.

countries will be responsible for over the half of the global energy demand rise<sup>10</sup>, it is worth to examine their energy policies.

The aim of this paper is to analyse the challenges to the energy security of China and India in the 21<sup>st</sup> century and their response in the form of energy diplomacy. I will argue that the energy diplomacy of China and India allowed oil companies from both countries to become important players in the market but only indirectly increased the energy security of their home countries. Contrary to the initial concerns, the energy diplomacy of China and India has neither changed the structure of the market nor challenged the principles of their foreign policies.

This paper has the following structure. First, I will discuss the importance of energy security and energy diplomacy for modern states. Second, I will look at the challenges facing the energy security of India and China, concentrating on oil, which has been traditionally perceived as a politically significant commodity<sup>11</sup>. In the third part I will compare the energy diplomacy of both countries and look at the impact of their energy diplomacies on the global oil market.

### **1. Energy security and energy diplomacy**

The issue of energy security was raised for the first time by Winston Churchill in the early 20<sup>th</sup> century as the British Navy changed the fuel it used from coal to oil. Churchill argued in 1913 that “safety and certainty in oil lie in variety and variety alone”<sup>12</sup>. Energy security became a broad discussed issue first in 1970s. Despite the fact that in the 1950s and the 1960s the oil supply from the Middle East (the key production and export region) was cut several times, oil importers did very little to improve their energy security<sup>13</sup>. The oil embargo of the Organization of Arab Petroleum Exporting Countries (AOPEC) of 1973 was a shock for the international community. It was the first successful use of oil as a political weapon. Together with a wave of nationalization of oil assets in the Middle East (and all over the world), it changed the balance of power in international political economy, making oil exporters fabulously rich. Only a few years later, in 1979, in the consequence of the Iranian revolution, oil prices rose again<sup>14</sup>.

The experience of the 1970s has determined the understanding of energy security for decades. Today there are plenty definitions of energy security.

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<sup>10</sup> IEA (International Energy Agency), *World Energy Outlook 2007*, Paris 2007, p. 118.

<sup>11</sup> P. Stevens, *Oil Wars, Resource Nationalism and the Middle East*, in P. Andrews-Speed (ed.), *International Competition for Resources: the Role of Law, the State and of Markets*, Dundee, Dundee University Press, 2008, pp. 11-44.

<sup>12</sup> W. Churchill, *The real trouble with oil*, in „The Economist”, Apr 28<sup>th</sup> 2005, see: [www.economist.com/node/3910260](http://www.economist.com/node/3910260) (accessed on 28 July 2016).

<sup>13</sup> M. L. O’Sullivan, *The Entanglement of Energy, Grand Strategy, and International Security*, in A. Goldthau (ed.), *The Handbook of Global Energy Policy*, Chichester, John Wiley&Sons Ltd, 2013, p. 37.

<sup>14</sup> A. Ehteshami, *Security and Strategic Trends in the Middle East*, in D. Held, K. Ulrichsen (eds.), *The Transformation of the Gulf Politics, Economics and the Global Order*, Routledge, New York, 2012, p. 266.

Benjamin K. Sovacool counted 45 of them<sup>15</sup>. “There is no common interpretation”<sup>16</sup>, and the concept is „abstract, elusive, vague, inherently difficult and blurred”<sup>17</sup>. Some authors even reduce the issue of energy security to imperfect market competition and advocate support for free market as the best defence against state intervention<sup>18</sup>.

The IEA defines energy security as “the uninterrupted availability of energy sources at an affordable price”<sup>19</sup>. Robert Mabro, the founder and long-term director of the Oxford Institute for Energy Studies argues: “Security is impaired when supplies are reduced or interrupted in some places to an extent that causes a sudden, significant and sustained increase in prevailing prices”<sup>20</sup>. I will follow Mabro’s definition as the one best responding to the challenges facing China and India.

The experience of G7 countries shows that the improvement of energy security may be achieved by different means. Generally, industrialized countries have reduced the energy intensity of their economies, substituted oil by other energy sources and developed energy diplomacy to get access to oil reserves of other countries<sup>21</sup>. For India and China the “uninterrupted availability” and the “affordable price” are equally important aspects of energy security. Both are still developing countries. India has already experienced a currency crisis in 1991, which was partly the result of a rise of its spending on oil. In the budget year 1990/1991, the value of imported petroleum jumped by 2 billion USD compared to the previous year to a total of 5.7 billion USD. The reason behind this was a rise of the volume of imported oil and petroleum products as well as a rise of prices in consequence of the military conflict in the Middle East<sup>22</sup>.

As there is still no substitute for petroleum products in the transport sector, all countries remain “addicted to oil”<sup>23</sup>. Most countries have still not achieved

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<sup>15</sup> B. K. Sovacool, *Introduction. Defining, measuring, and exploring energy security*, in B. K. Sovacool (ed.), *The Routledge Handbook of Energy Security*, Routledge, New York, 2011, pp. 3-6.

<sup>16</sup> A. Checchi, A. Behrens, Ch. Egenhofer, *Long-Term Energy Security Risks for Europe: A Sector-Specific Approach*, CEPS Working Document, 2009, p. 1.

<sup>17</sup> A. Löschel, U. Moslener, D. T. G. Rübhelke, *Indicators of energy security in industrialised countries*, in „Energy Policy”, no. 38/2010, p. 1665; see F. Ciută, *Conceptual Notes on Energy Security: Total or Banal Security?*, in „Security Dialogue”, vol. 41, no. 2, 2010, pp. 123-144.

<sup>18</sup> P. Noel, *Is energy security a political, military or market problem?* An online Q&A, in „Financial Times”, January 10, 2008, see: [www.ft.com/cms/s/2/fd6ef84a-bf85-11dc-8052-0000779fd2ac.html](http://www.ft.com/cms/s/2/fd6ef84a-bf85-11dc-8052-0000779fd2ac.html) (accessed on 28 July 2016).

<sup>19</sup> IEA, *What is energy security?*, see [www.iea.org/topics/energysecurity/subtopics/whatisenergysecurity/](http://www.iea.org/topics/energysecurity/subtopics/whatisenergysecurity/) (accessed on 28 July 2016).

<sup>20</sup> R. Mabro, *On the security of oil supplies, oil weapons, oil nationalism and all that*, in „OPEC Energy Review”, vol. 32, no. 1, 2009, pp. 1-12.

<sup>21</sup> J. S. Duffield, *Fuels Paradise Seeking Energy Security in Europe, Japan, and the United States*, John Hopkins University Press, Baltimore 2015.

<sup>22</sup> V. Cerra, S. Ch. Saxena, *What Caused the 1991 Currency Crisis in India?*, IMF Staff Papers, vol. 49, no. 3, 2002, p. 403.

<sup>23</sup> FT View, *Sinking deeper into our addiction to oil*, in „Financial Times”, July 10, 2016, see: [www.ft.com/cms/s/0/2e2be2fa-450a-11e6-9b66-0712b3873ae1.html#axzz4FnHiA7Tk](http://www.ft.com/cms/s/0/2e2be2fa-450a-11e6-9b66-0712b3873ae1.html#axzz4FnHiA7Tk) (accessed on 28 July 2016).

“energy independence” and have to accept “interdependence”. Most countries develop energy diplomacy, which just as energy security does not have a single definition. It has different goals in countries being energy exporters than in countries being energy importers<sup>24</sup>. Since India and China are oil importers, I will follow the broadly accepted definition of Andreas Goldthau, who defines energy diplomacy as “the use of foreign policy to secure access to energy supplies abroad and to promote (mostly bilateral, that is, government to government) cooperation in the energy sector. This definition suggests that the primary units of analysis are states or states actors, that the primary driver behind the conclusion of oil and gas deals is not necessarily maximizing business opportunities but national security goals; and that the underlying cost-benefit calculations do not follow an economic logic but rather a political one”<sup>25</sup>.

## 2. Challenges facing energy security of India and China

China and India rose in the 21<sup>st</sup> century to the position of economic powers<sup>26</sup>. China became the largest and India the third largest energy consumer in the world, and the two countries are also the second and fourth crude oil and petroleum products consumers in the world in 2015 respectively.

The challenges for the energy security of the two countries may be divided into two groups. The first one is their dependence on foreign oil (the external dimension). The second group of challenges are those of domestic nature (vulnerability of power sector, environmental costs, etc.)<sup>27</sup>. Energy security has been increasingly often seen a broader sense, as “encompassing technology, fuels, trade, behaviour, institutions the environment, and education”<sup>28</sup>. This paper focuses on the external dimension.

The main challenge for India and China lays in their change of position in the market toward large importers and high dependence on the global oil market, which they cannot control. In 2001, China’s share in the global oil consumption was only 6.6% and India’s was 2.8%<sup>29</sup>. But already in 2015, China’s share in the

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<sup>24</sup> M. B. Uludağ, S. Karagül, G. Baba, *Turkey's Role in Energy Diplomacy from Competition to Cooperation: Theoretical and Factual Projections*, in „International Journal of Energy Economics and Policy”, vol. 3, Special Issue, 2013, p. 102; C. Zhang, *The Domestic Dynamics of China's Energy Diplomacy*, World Scientific Publishing, Singapore 2015, p. 7.

<sup>25</sup> A. Goldthau, *Energy Diplomacy in Trade and Investment of oil and gas*, in A. Goldthau, J.M. Witte (eds.), *Global energy governance, the new rules of the game*, Berlin, Brooking Institution Press, 2010, p. 28.

<sup>26</sup> D. Shambaugh, *China Goes Global: The Partial Power*, New York, Oxford University Press, 2013; A. Panagariya, *India: The Emerging Giant*, New York, Oxford University Press, 2008.

<sup>27</sup> A. B. Kennedy, *China's New Energy-Security Debate*, in „Survival: Global Politics and Strategy”, vol. 52, no. 3, 2010, pp. 137-158; H. Singh, *India Debates Its Energy Security*, in „Journal Of Law And Public Policy”, vol. 1, no. 1, 2014, see: [lawjournalindia.in/index.php/2015-02-19-19-48-03/issue1-vol-1/114-india-debates-its-energy-security.html](http://lawjournalindia.in/index.php/2015-02-19-19-48-03/issue1-vol-1/114-india-debates-its-energy-security.html) (accessed on 28 July 2016).

<sup>28</sup> B. K. Sovacool, V. Vivoda, *A comparison of Chinese, Indian, and Japanese. Perceptions of Energy Security*, in „Asian Survey”, vol. 52, no. 5, 2012, p. 951.

<sup>29</sup> *BP statistical review of world energy June 2002*, p. 9.

global oil consumption was 12.9% and India's was 4.5%<sup>30</sup>. Most of their imports come from the Middle East. Already in the early 21<sup>st</sup> century, as demand in China and India started to rise, this dependence was seen as a threat to energy security<sup>31</sup>. Another concern for the two countries is the security of sea lines. Oil transported from the Persian Gulf has to go through the Strait of Hormuz, and on the way to China it also needs to pass through the Strait of Malacca<sup>32</sup>.

In both India and China the energy mix is dominated by coal. In 2013, coal was responsible for 44% of total energy consumption in India, biomass and waste for 24%, and petroleum and other liquids for 23%<sup>33</sup>. In China, the role of coal is even greater. The share of coal in the Chinese energy supply was 66% in 2012. The second most important resource was oil, with 20%<sup>34</sup>. In India, the current level of oil production is higher than in the early 21<sup>st</sup> century, but there has been a dramatic rise of consumption and the gap between local supply and demand has widened. The U.S. Energy Information Administration (EIA) predicts that the demand will rise and the gap will widen further in the coming years. The reasons for this are as follows: India's transportation and industrial sectors continue to expand, the prices are relative low, government investments in roads and highways, and state support for local manufacturing. Similar problems face the government of China. In the last 20 years, China enjoyed a rise of oil production by 50%. Furthermore, the forecasts concerning production are optimistic. But the demand rise was much faster. China was responsible for a substantial part of the global oil consumption growth in the 21<sup>st</sup> century. After a year-to-year maximum consumption growth in 2010 by 11%, Chinese demand growth slowed down to 4% in 2014 against 2013. The reason for that are: global economic and financial downturn, government efforts to reduce investments and capacity overbuilding in certain industries (especially energy intensive ones). This impact of economic downturn and restriction of investments is very well visible on the product market. In 2014 for the first time in two decades consumption of diesel went down. On the other hand the gasoline consumption associated with the use of private cars enjoys still a robust growth. Governments of both countries try to minimize dependence on foreign oil imports investing in better energy efficiency of their economies and alternative sources of energy like nuclear energy or renewable. Both countries are heavily dependent on oil imports from the Middle East. 59% of Indian oil imports came from this region (data for 2015) and 52% of Chinese imports (data for 2014). For both countries Saudi Arabia is the biggest supplier, delivering 20% of oil imported by India and 16% of

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<sup>30</sup> BP Statistical Review of World Energy June 2016, p. 11.

<sup>31</sup> R. Manning, *The Asian energy predicament*, in „Survival”, vol. 42, no. 3, 2000, pp. 73-88.

<sup>32</sup> U.S. Energy Information Administration (it will be further cited as EIA), *World oil transit chokepoints critical to global energy security*, 1 December 2014, see: [www.eia.gov/todayinenergy/detail.cfm?id=18991](http://www.eia.gov/todayinenergy/detail.cfm?id=18991) (accessed on 28 July 2016).

<sup>33</sup> EIA, *India*, June 14<sup>th</sup> 2016, see: [www.eia.gov/beta/international/analysis.cfm?iso=IND](http://www.eia.gov/beta/international/analysis.cfm?iso=IND) (accessed on 28 July 2016).

<sup>34</sup> EIA, *China*, May 14<sup>th</sup>, 2015, see: [www.eia.gov/beta/international/analysis.cfm?iso=CHN](http://www.eia.gov/beta/international/analysis.cfm?iso=CHN) (accessed on 28 July 2016).

oil imported by China<sup>35</sup>. An important guideline for the situation in Chinese energy sector in the next years is the 13<sup>th</sup> Five-Year Plan. It is crucial for Chinese energy sector on three levels. First, there is question of transformation of the Chinese economy toward a consumer-driven development path and of the future growth rates (government plans 6.5% p.a. for the period covered by the 13<sup>th</sup> Five-Year Plan). Second, the Chinese economy is already in the process of rebalancing. Demand for light petroleum products (jet fuel, gasoline) and petrochemicals is on the rise. On the other hand, prospects for diesel are pessimistic. Third, environment protection is of high priority for the Chinese government. 10 out of 25 numerical targets in the 13<sup>th</sup> Five-Year Plan are related to the environment. It is the aim of the Chinese government to reduce energy intensity of the economy by 15%. In the 2010–2015 period, China managed to reduce its energy intensity by 18.2%. The plan also reflects the country's desire to shift from oil based fuels in the transport sector to alternative sources of energy<sup>36</sup>. The high economic growth in India and the rebalancing of the Chinese economy may indicate that India will overtake China as the main source of demand growth in the oil market<sup>37</sup>.

Self-reliance is among the most important goals for both countries' energy policies. China enjoyed it in the 1970s and the 1980s, after the discovery of huge oil fields such as Daqing (in 1959), Shengli (in 1963), Dagang (in 1964), and Liaohe (in 1969). It was also able to export oil in substantial quantities at that time. Even Chinese membership in Organization of the Petroleum Exporting Countries (OPEC) was discussed<sup>38</sup>. China became an oil importer again in 1993. In consequence, it had to change its energy policy. This process accelerated in the 21<sup>st</sup> century as oil imports and prices rose. Raja Mohan and Lydia Powell summarize the oil strategy of China as follows: "China's oil strategy highlighted diversification of supply sources, co-developing oil and gas wells with other countries, cutting out unreliable oil transportation routes, and developing a single dedicated destination for oil produced by Chinese companies"<sup>39</sup>. As regards India, documents such as the Hydrocarbon Vision 2025 commissioned by the prime minister of India in 2000 recommend "intensification of exploration efforts and securing acreages in countries in countries having high attractiveness for ensuring sustainable long-term supplies". Iraq, Iran, Russia and North Africa were on the list of potential investment destinations.

For both countries, energy security is a part of broader socio-economic goals. In the case of China, energy policy has three main goals. First, the government tries to ensure security of supply. Second, the government tries to

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<sup>35</sup> EIA, *India*, June 14<sup>th</sup>, 2016, *op. cit.*; EIA, *China*, May 14<sup>th</sup>, 2015, *op. cit.*

<sup>36</sup> M. Meidan, *China's 13th Five-Year Plan: Implications for Oil Markets*, Oxford Energy Comment, 2016.

<sup>37</sup> A. Sen, A. Sen, *India's Oil Demand: On the Verge of 'Take-Off'?*, OIES Paper: WPM 65, 2016.

<sup>38</sup> M. Meidan, *The structure of China's oil industry: Past trends and future prospects*, OIES Paper: WPM 66, pp. 4-8.

<sup>39</sup> C. R. Mohan, L. Powell, *Energy Rivalry between India and China: Less than Meets the Eye*, in D. Steven, E. O'Brien, B. Jones (eds.), *The new politics of strategic resources. Energy and food security challenges in the 21<sup>st</sup> century*, Washington D.C., Brookings Institution, 2015, pp. 147-148.

secure cheap energy supply to secure stable and high economic growth. Third, the Chinese government tries to implement energy policies that are neutral for the environment. But as David Robinson suggests, there are tensions between these three goals. Oil and natural gas are more environmentally friendly than locally produced coal. There are especially strong concerns about the future supply of oil, however. The main reason is not the current level of imports but much rather forecasts concerning its future level, which say that China will import around 12.5 mln b/d in 2035, which will put the country in a similar situation to that of the United States and Western European countries after 1973<sup>40</sup>. Due to fast growth in motorization<sup>41</sup> and reduction of the United States' oil imports in consequence of the US energy revolution, it is already in 2013 that "China's net imports of petroleum and other liquids exceeded those of the United States on a monthly basis, making it the largest net importer of crude oil and other liquids in the world"<sup>42</sup>. As Andrew B. Kennedy suggests, in achieving energy security the Chinese government undertook four steps: 1) striking bilateral deals with oil producing countries and giving support to NOCs; 2) the desire to diversify sources of oil supply to China; 3) a build-up of naval forces to strength naval capabilities; 4) development of strategic petroleum reserves<sup>43</sup>. The challenges that face India as well as the country's response are remarkably similar<sup>44</sup>.

Both countries also have a similar structure of the industry. In the case of India, the Ministry of Petroleum and Natural Gas (MOPNG) is responsible for this sector. It regulates the entire value chain of the oil sector, including exploration and production (E&P), refining, supply, and marketing. India has two National Oil Companies (NOCs): Oil and Natural Gas Corporation (ONGC), which is the biggest oil company in India, and Oil India Limited (OIL). A few private companies, like Reliance Industries (RIL) and Essar Oil, have emerged as important players in India's oil industry in the past decade, but they focus on refinery business. Thanks to state support, they invested heavily in refineries in the last two decades and transformed India from net petroleum products importer into net petroleum products exporter<sup>45</sup>. In China, the main body responsible for the petroleum sector is The National Development and Reform Commission (NDRC),

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<sup>40</sup> D. Robinson, *China's growing energy demand: some international implications*, 2013, see: [www.oxfordenergy.org/wpcms/wp-content/uploads/2013/12/Chinas-growing-energy-demand.pdf](http://www.oxfordenergy.org/wpcms/wp-content/uploads/2013/12/Chinas-growing-energy-demand.pdf) (accessed on 28 July 2016), p. 7.

<sup>41</sup> W.-S. Ng, L. Schipper, Y. Chen, *China Motorization Trends, New Directions for Crowded Cities*, in „The Journal of Transport and Land Use”, vol. 3, no. 3, 2010, pp. 5-25.

<sup>42</sup> EIA, *China is now the world's largest net importer of petroleum and other liquid fuels*, March 24, 2014, see: [www.eia.gov/todayinenergy/detail.cfm?id=15531](http://www.eia.gov/todayinenergy/detail.cfm?id=15531) (accessed on 28 July 2016).

<sup>43</sup> A. B. Kennedy, *China's Search for Oil Security: A Critique*, in D. Steven, E. O'Brien, B. Jones (red.), *The new politics of strategic resources. Energy and food security challenges in the 21<sup>st</sup> century*, Brookings Institution, Washington D.C., 2015, pp. 23-39.

<sup>44</sup> *India's energy security new opportunities for a sustainable future*, The Energy and Resources Institute (TERI), New Delhi, 2009; Planning Commission, *Integrated Energy Policy: Report of the Expert Committee*, New Delhi, 2006.

<sup>45</sup> EIA, *India*, June 14th 2016, see [www.eia.gov/beta/international/analysis.cfm?iso=IND](http://www.eia.gov/beta/international/analysis.cfm?iso=IND) (accessed on 28 July 2016).

a department of China's State Council. It is responsible for policymaking, planning and regulation of the oil sector. Other ministries such as the Ministry of Commerce, the Ministry of Land and Resources, the Ministry of Environmental Protection, and the State Oceanic Administration oversee certain areas of the oil industry. China established three NOCs: China National Petroleum Corporation (CNPC), the China Petroleum and Chemical Corporation (Sinopec), and China National Offshore Oil Corporation (CNOOC). After several reforms in the 1990s, they are today vertically integrated companies with publicly-listed subsidiaries<sup>46</sup>. In this context it is important to mention the declaration of President Hu Jintao, where he argued that oil and finance constitute two components of Chinese economic security<sup>47</sup>. In November 2013, China's Central Committee has announced a plan to give a "decisive" role to markets in its economy by 2020<sup>48</sup>. As this short analysis of the structure of the energy sectors of the two countries, in China it is dominated by NOCs, while in India state-controlled and private-owned companies coexist with each other.

### 3. Oil diplomacy

The market proved to be an effective regulator of oil affairs. Although it does not guarantee price stability, there is a consensus that it works properly or at least that it is much more sustainable than the previous oil regime, when OPEC controlled the market<sup>49</sup>. Despite that, China and India decided to develop energy diplomacy, which is shown in many statements of the countries' state leaders and in official documents<sup>50</sup>. For many authors, the energy diplomacy of India and China presents a challenge for market forces and promotion of neo-mercantilist policy<sup>51</sup>. Neo-mercantilism is defined as "state-directed efforts aimed at making asymmetrical economic gains at the expense of competitors" that runs against "liberal assumptions and expectations"<sup>52</sup>. Neo-mercantilism sees international energy policy as a zero sum game, where a single country struggles to achieve relative gains at the expense of other countries. Countries that follow the neo-mercantilist approach perceive markets as insufficient to provide the required energy supply and engaged high politics to achieve energy security. In

<sup>46</sup> EIA, *China*, May 14<sup>th</sup>, 2015, see [www.eia.gov/beta/international/analysis.cfm?iso=CHN](http://www.eia.gov/beta/international/analysis.cfm?iso=CHN) (accessed on 28 July 2016).

<sup>47</sup> H. H. Lai, *China's Oil Diplomacy: Is It a Global Security Threat?* in „Third World Quarterly”, vol. 28, no. 3, 2007, p. 522.

<sup>48</sup> I. Dreyer, G. Stang, *Energy moves and power shifts EU foreign policy and global energy security*, EU Institute for Security Studies Report, 2014, p. 8.

<sup>49</sup> B. Fattouh, *An Anatomy of the Crude Oil Pricing System*, OIES Paper: WPM 40, 2011.

<sup>50</sup> H. Zhao, *China and India: The Quest for Energy Resources in the 21st Century*, Routledge, New York, 2013, pp. 58-61.

<sup>51</sup> H.- C. Yeh, C.-W. Yu, *China's Energy Diplomacy: SOE Relations in the Context of Global Distribution and Investment Pattern*, in „Advances in Applied Sociology”, vol. 2, no. 4, 2012, pp. 325-343; A. Phillips, *A dangerous synergy: energy securitization, great power rivalry and strategic stability in the Asian century*, in „The Pacific Review”, vol. 26, no. 1, 2013, p. 18.

<sup>52</sup> Ch. E. Ziegler, R. Menon, *Neomercantilism and Great-Power Energy Competition in Central Asia and the Caspian*, in „Strategic Studies Quarterly”, vol. 8, no. 2, 2014, p. 17.



consequence, countries following the neo-mercantilist approach are disruptive for the market forces, open market structure, transparency of transactions and economic accountability. Neo-mercantilism expresses the desire for state material capacity to grow, maximize state power and wealth as well as reduce the state's vulnerability against other actors<sup>53</sup>. Expansion of Chinese oil companies was even perceived as a challenge to liberal capitalism and a form of promotion of the Chinese economic model (Beijing Consensus)<sup>54</sup>. Other authors refuse the division of neo-mercantilism vs. liberal approach to the energy issue and see China as a pragmatic player who wisely reacts to local circumstances<sup>55</sup>. Daniel Yergin et al. observed that China's and India's desire to secure energy security comes close to the concerns Western European countries and the United States had back in the 1970s<sup>56</sup>. But China and India are not members of the IEA, the most important organization of oil importing countries. The main reasons for this are securitization of energy issues in both countries and economic nationalism<sup>57</sup>. As Daniel Yergin argues, "It would be wiser – and indeed it is urgent – to engage these two giants in the global network of trade and investment rather than see them tilt toward a mercantilist, state-to-state approach. Engaging India and China will require understanding what energy security means for them"<sup>58</sup>.

Prime Minister Manmohan Singh pointed out in 2005 that India's energy diplomacy is to coordinate the following activities: 1) the investment of Indian companies (public and private) in overseas mining projects; 2) the construction of pipelines; 3) the conclusion of bilateral agreements between the Government of India and the governments of other countries and securing the supply of crude oil and natural gas. The aim of energy diplomacy is to help Indian companies participating in tenders for exploitation of energy resources abroad as well as to diversify sources of supply. It should lay the foundations for future cooperation with the countries exporting and importing energy resources and foster the exchange of investment and cooperation in the field of technology<sup>59</sup>. The history of energy diplomacy of India goes back to the 1950s. ONGC has played a central role in it. Today it is internationally active through its subsidiary ONGC Videsh Ltd. (OVL). In 1958 ONGC considered exploration of oil in Nepal, but for political

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<sup>53</sup> H.- C. Yeh, C.-W. Yu, *op. cit.*, pp. 325-326.

<sup>54</sup> V. Vivoda, *China challenges global capitalism*, in „Australian Journal of International Affairs”, vol. 63, no.1, 2009, pp. 22-40.

<sup>55</sup> M. Gueldry, W. Liang, *China's Global Energy Diplomacy: Behavior Normalization Through Economic Interdependence or Resource Neo-mercantilism and Power Politics?*, in „Journal of Chinese Political Science”, vol. 21, no. 2, 2016, pp. 217-240.

<sup>56</sup> D. Yergin, D. Eklöf, J. Edwards, *Fuelling Asia's Recovery*, in „Foreign Affairs”, vol. 77, no. 2, 1998, pp. 34-50.

<sup>57</sup> J. D. Wilson, *Multilateral Organisations and the Limits to International Energy Cooperation*, in „New Political Economy”, vol. 20, no. 1, 2015, pp. 85-106.

<sup>58</sup> D. Yergin, *Ensuring Energy Security*, in „Foreign Affairs”, vol. 85, no. 2, 2006, pp. 77-78; see: F. Verrastro, S. Ladislawa, *Providing Energy Security in an Interdependent World*, in „The Washington Quarterly”, vol. 30, no. 4, 2007, p. 95.

<sup>59</sup> T. Madan, *India's International Quest for Oil and Natural Gas: Fueling Foreign Policy?* in „India Review”, vol. 9, no. 1, 2010, pp. 5, 10.

reasons this project stalled. In the 1950s and the 1960s, the company received a proposal for cooperation from Kuwait, Saudi Arabia and Iran. But the cooperation was not undertaken because there were worries that it could negatively influence relations with the United States, which was the biggest provider of Official Development Assistance (ODA) to India at that time. There was also strong belief that oil would be found at home. Letter ONGC decided to take together with AGIP, Philips and NIOC a stake in an offshore lease in Iran. That was the first contract signed with Iran/NIOC. In 1973 ONGC was also awarded service contracts in Iraq and Tanzania. But it is only in the 21<sup>st</sup> century that full-scale ONGC expansion began<sup>60</sup>, supported by the Indian government<sup>61</sup>. In the early 21<sup>st</sup> century ONGC has acquired assets in a number of countries, including Angola, Libya, Iran, Iraq, Myanmar, Russia, Sudan, Syria, Venezuela, and Vietnam<sup>62</sup>. Although the company is of crucial importance to India's oil policy it enjoys growing independence. But at the same time the government has still formal and informal influence on the company's policy, especially in such aspects as: personal, production allocations and targets, day-to-day processes, oversight, politics<sup>63</sup>. The important issue is that the price reform gave ONGC much more freedom in its corporate policy<sup>64</sup>.

In the middle of the first decade of 21<sup>st</sup> century, ONGC as well as other Indian oil companies substantially improved their management of projects in face of Chinese competition<sup>65</sup>. But in comparison to China, there is still a broad set of institutions responsible for realization of energy diplomacy, which makes its effective implementation difficult<sup>66</sup>. Behind the struggle for global expansion there is also deep disagreement about its sense. Its supporters suggest that it offers a chance to acquire cheaply rights for oil exploration abroad and ensure cheap and reliable oil supply. But others indicate that ONGC only takes advantage of the worries about energy security present in India to receive state support. The oil that it produces abroad is actually not delivered to India but instead sold in the global market. The government also prefers that ONGC concentrates more on exploration and development of local resources instead of foreign investments. It is worried that global expansion reduces the resources (technical, financial, human) available for local operations. The next argument against ONGC expansion is that the terms that the company agrees to are uneconomic. Furthermore, ONGC has insufficient technological knowledge to take full advantage of exploration rights that it acquires abroad<sup>67</sup>.

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<sup>60</sup> T. Madan, *India's ONGC: Balancing Different Roles, Different Goals*, The James A. Baker III Institute For Public Policy Rice University, 2007, p. 50.

<sup>61</sup> Idem, *op. cit.*, in „India Review”, vol. 9, no. 1, 2010, pp. 2–37.

<sup>62</sup> Idem, *op. cit.*, The James A. Baker III Institute For Public Policy Rice University, 2007, p. 23.

<sup>63</sup> *Ibidem*, pp. 27–46.

<sup>64</sup> B. Fattouh, A. Sen, A. Sen, *Diesel Pricing Reforms in India – a Perspective on Demand*, Oxford Energy Comment, 2013.

<sup>65</sup> K.-W. Paik, V. Marcel, G. Lahn, J. V. Mitchell, E. Adylov, *Trends in Asian NOC investment abroad*, Chatham House, Working Background Paper, 2007.

<sup>66</sup> G. Bahgat, *India's Energy Security*, in „Minerals & Energy”, vol. 21, no. 3–4, 2006, p. 35.

<sup>67</sup> T. Madan, *op. cit.*, The James A. Baker III Institute For Public Policy Rice University, pp. 51–53.

At the same time, Indian authorities seek to protect the existing ways of energy supply and create new ones. They seek to increase the country's influence in the Indian Ocean region, which could strengthen India's international position<sup>68</sup>. For this purpose, they are developing the Navy so that it becomes the dominant power in the Indian Ocean. India's fears arise from the dependence on oil supply from the Gulf, which is separated from the Indian Ocean by the Strait of Hormuz, one of most important choke points globally. In response to these challenges, the government is considering the development of a pipeline system connecting India with countries rich in energy resources. India wishes to reduce dependence on natural gas in liquid form (Liquefied Natural Gas, LNG) by developing new gas pipelines. There are three proposals for gas pipelines: Iran–Pakistan–India (IPI), Turkmenistan–Afghanistan–Pakistan–India (TAPI) and Bangladesh–Myanmar–India (MBI). But the implementation of each of these projects faces a number of problems, mainly related to security issues<sup>69</sup>.

One of the major obstacles for ONGC global expansion is the need for Indian companies to acquire approval from the Reserve Bank of India for all investments worth more than 45 million USD, which effectively means that it is required for all ONGC investments. Second, the government of India blocked several investments because it had security concerns (Sudan, Nigeria) and was worried whether the next governments would approve the contract (the case of Nigeria). Third, the government introduced economic requirements so as to not overpay for assets. One important element observed in India's energy diplomacy is the commitment of individual ministers to the development of energy diplomacy<sup>70</sup>.

To summarize the relations between the government and oil companies in India it is worth pointing out that: "Companies like ONGC have benefited from the Indian government's efforts, and simultaneously served as an indispensable part of the government's energy strategy abroad."<sup>71</sup>

In academic literature there are two perspectives on Chinese energy diplomacy. The first one is the liberal integrationist view saying that China is shifting from neo-mercantilism toward recognition of the role of the market. The second perspective is a realist perspective. The authors belonging to this group argue that Chinese diplomacy aims at strategic balancing with resource rich countries (especially Russia) and see increased strategic presence in the area from the Persian Gulf to North-eastern Asia<sup>72</sup>.

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<sup>68</sup> J. Zajączkowski, *India's Foreign Policy following the end of the Cold War*, in J. Zajączkowski, J. Schottli, M. Thapa (eds.), *India in the Contemporary World: Polity, Economy and International Relations*, Routledge, London, New York, New Delhi, 2014, pp. 265–307; E. Albert, *Competition in the Indian Ocean*, CFR Backgrounders, May 19, 2016, see [www.cfr.org/regional-security/competition-indian-ocean/p37201](http://www.cfr.org/regional-security/competition-indian-ocean/p37201) (accessed on 28 July 2016).

<sup>69</sup> S. S. Kulkarni, *India's Pipeline Diplomacy: Case of Lost Opportunities*, ISSSP Reflections, no. 4, 2013; M. Lall, *Indo-Myanmar Relations in the Era of Pipeline Diplomacy*, in „Contemporary Southeast Asia”, vol. 28, no. 3, 2006, pp. 424–446.

<sup>70</sup> T. Madan, *op. cit.*, The James A. Baker III Institute For Public Policy Rice University, pp. 53–54, 60.

<sup>71</sup> *Ibidem*, p. 56.

<sup>72</sup> R. Dannreuther, *China and global oil: vulnerability and opportunity*, in „International Affairs”, 2011, vol. 87, no. 6, pp. 1346–1347.

The key driver of Chinese energy diplomacy was fear about the stability of oil supply from the Middle East and about the consequences of resource nationalism that rose in the early 21<sup>st</sup> century in many oil exporting countries<sup>73</sup>. The second important challenge for energy security that Chinese energy diplomacy should mitigate is dependence of Chinese oil imports on sea transport through *choke points*<sup>74</sup>, especially the *Strait of Hormuz and the Strait of Malacca*. In 2009 CNPC signed a memorandum of understanding with Myanmar that opened a way to build parallel oil and gas pipelines to connect the Chinese province Yunan with the Indian Ocean. The pipeline also reduces the travel distance by 1200 km<sup>75</sup>. But it has limited capacity and only reduces the “Malacca dilemma”. Plenty of other proposals are currently under discussion, with a canal through southern Thailand or a pipeline across Malaysia being the most ambitious and least probable at once<sup>76</sup>. China also develops the People’s Liberation Army Navy. One of the indicated reasons for this is the ability to protect sea lines. China is worried that the United States Navy would be able to cut oil supply to China<sup>77</sup>.

*Apart from investing in new pipelines, Chinese oil diplomacy uses two instruments: direct investments in foreign upstream assets and “loans-for-oil” deals with countries such as Brazil, Angola, Venezuela and Russia, among others*<sup>78</sup>.

The strong government support the Chinese NOCs enjoy has been seen by oil companies from other countries as undermining the “level playing field”<sup>79</sup>. But despite this support, they cannot be seen as simple tools of Chinese foreign policy. They are autonomous entities in which commercial and strategic interests intersect<sup>80</sup>. Besides, oil companies from other countries enjoy state support as well<sup>81</sup>. CNPC’s international expansion started in 1992, when it acquired the rights to develop blocks in the aging Talala oil field in Peru. “Ironically, the government planners took little notice of the company’s first forays into Peru, Sudan and Kazakhstan until the mid-1990s. A contingent of the country’s top leaders did not envision overseas upstream investments as a sound strategy, and instead even

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<sup>73</sup> I. Dreyer, Gerald Stang, *op. cit.*, pp. 5-6.

<sup>74</sup> D. Robinson, *op. cit.* p. 20.

<sup>75</sup> A. B. Kennedy, *China’s Search for Oil Security: A Critique*, p. 29.

<sup>76</sup> S. Chen, *China’s Self-Extrication from the “Malacca Dilemma” and Implications*, in „International Journal of China Studies”, vol. 1, no. 1, 2010, pp. 1-24; Ch. Len, *China’s 21st Century Maritime Silk Road Initiative, Energy Security and SLOC Access*, in „Maritime Affairs: Journal of the National Maritime Foundation of India”, vol. 11, no. 1, 2015, pp. 1-18; G. S. S. Khurana, *China, India and “Maritime Silk Road”: Seeking a Confluence*, in „Maritime Affairs: Journal of the National Maritime Foundation of India”, vol. 11, no. 1, 2015, pp. 19–29.

<sup>77</sup> T. M. Kane, *Chinese Grand Strategy and Maritime Power*, Routledge, New York London 2016; S. Yoon, *Implications of Xi Jinping’s “True Maritime Power”*, in „Naval War College Review”, vol. 68, no. 3, 2015, pp. 40-63.

<sup>78</sup> D. Robinson, *op. cit.*, p. 20.

<sup>79</sup> R. Dannreuther, *op. cit.*, pp. 1345-6.

<sup>80</sup> A. B. Kennedy, *China’s Search for Oil Security: A Critique*, p. 25.

<sup>81</sup> G. Bahgat, *American Oil Diplomacy in the Persian Gulf and the Caspian Sea*, University Press of Florida, Gainesville 2003.

emphasized continued domestic investments”<sup>82</sup>. Only when the “going out” strategy was generated as a part of national strategy in 1997 did the expansion of oil companies start to enjoy interest of state elites. The international expansion of CNPC, Sinopec and CNOOC became a part of the “going out” strategy. The Chinese government is determined to transform local companies into global players. It is convinced that not only should China be an attractive place for foreign investments but Chinese companies should also invest abroad. In this context it is frequently stressed that Chinese direct investments have the goal to build a Chinese sphere of influence. But a closer analysis shows that Chinese NOCs have strong commercial interests in overseas investments. These interests do not contradict the interest of the Chinese state but coexist with each other<sup>83</sup>. As an IEA report from 2011 shows, Chinese NOCs enjoy high levels of independence from government intervention, and their investments are motivated by economic factors<sup>84</sup>.

Chinese energy diplomacy is regionally diversified. The areas of interest include: the Middle East, Africa, Latin America, Russia and Central Asia. In the Middle East, the biggest partner for China is the Kingdom of Saudi Arabia (KSA). It is interesting to point out that Chinese–Saudi diplomatic relations were first established in 1990. Today there are frequent top-level summits between both countries and there is intensive economic cooperation. But China does not restrict its engagement in the region to the KSA. Iran – where a huge contract to develop a Yadaravan field was signed – and Iraq (service contracts) are the focus of Chinese energy diplomacy as well. But it is Chinese investments in Africa that enjoy the biggest interest. The list of Chinese companies investing in the energy sector in Africa is extremely long and includes Angola, Sudan, the Democratic Republic of Congo, and Gabon, among others. China has achieved a big success in this region. The reason is that the United States and the EU have distanced themselves from many African countries that violated human rights and where human rights concerns existed<sup>85</sup>. Chinese NOCs and the attractive conditions they offered filled the gap. Generally in 2002–2010 Chinese oil companies were engaged in 43 oil and gas acquisition deals worth 65 billion USD. In 2011–2012 they invested an additional 52 billion USD. In consequence, their oil production abroad rose from 140,000 b/d in 2000 to around 2 million b/d in mid-2013. “Loans-for-oil” played an especially important role in enhancing Chinese oil diplomacy during the crisis years of 2009–2010. Chinese banks gave credits to 9 countries, which were worth 77 billion USD. The credits are repaid with oil, priced in line with market prices. What is especially important, all of these countries were outside the Middle East<sup>86</sup>.

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<sup>82</sup> X. Xu, *Chinese NOCs' Overseas Strategies: Background, Comparison and Remarks*, The James A. Baker III Institute For Public Policy Rice University, 2007, p. 4.

<sup>83</sup> C.-s. Liou, *Bureaucratic Politics and Overseas Investment by Chinese State-Owned Oil Companies: Illusory Champions*, in „Asian Survey”, vol. 49, no. 4, 2009, pp. 671-672.

<sup>84</sup> J. Jiang, J. Sinton, *Overseas Investments by Chinese National Oil Companies. Assessing the drivers and impacts*, IEA Information Paper, 2011.

<sup>85</sup> See: H. H. Lai, *op. cit.*, pp. 522-29.

<sup>86</sup> A. B. Kennedy, *China's Search for Oil Security: A Critique*, pp. 25-26, 29.

There are four arguments against international expansion of Chinese NOCs. First, they do not automatically send oil produced abroad to China but instead sell it in the global market. Second, there is no convincing argument that oil produced by Chinese NOCs will be sold in China below market prices, and there is no guarantee that it will be available for China in the case of a global crisis. Third, there are some analyses that show Chinese NOCs have overpaid for foreign assets. It would mean that that they have enriched themselves and oil producing countries at the cost of China. It seems that it happened rather in the first phase of their global expansion. Fourth, they have invested in many countries being in conflict with the United States and Western European countries. Their investments may provoke challenges for Chinese foreign policy<sup>87</sup>.

Although the main goal of India's and China's energy diplomacy is to reduce the dependence on the Middle East, both of them appreciate the ability of Middle Eastern countries and especially the KSA to raise production and supply both countries with oil. It is also important to stress that the KSA is one of only a few countries able to provide oil in an amount required by such big economies like China or India. That is why both countries develop good, intensive and diversified relations with the KSA, which include also security issues<sup>88</sup>. It is also important to note that since the fall of oil prices started in June 2014, the share of the Middle East in global production has been rising, achieving levels last seen in the 1970s<sup>89</sup>.

As noted by Raja Mohan and Lydia Powell, the popular story is that India's and China's NOCs compete against each other. But this view neglects the fact that they also cooperate in South America, Africa, and the Middle East. They also signed many memoranda of understanding<sup>90</sup>. The reason for their cooperation was the wish to reduce their costs and the risk of overpaying for assets. But the cooperation is difficult; there is lack of trust between the partners and lack of institutional coordination<sup>91</sup>. Indian and Chinese companies are rather interested in cooperating with Western companies, which can offer them access to modern technologies<sup>92</sup>.

## Conclusions

China and India face two main challenges to their energy security from the international perspective. The first one is its dependence on sea lines. Most of the

<sup>87</sup> *Ibidem*, pp. 26-27.

<sup>88</sup> M. Quamar, *A New Direction for India-Saudi Arabia Ties*, in „The Diplomat”, March 10, 2016, see: [thediplomat.com/2016/03/a-new-direction-for-india-saudi-arabia-ties/](http://thediplomat.com/2016/03/a-new-direction-for-india-saudi-arabia-ties/); Naser M. Al-Tamimi, *China-Saudi Arabia Relations, 1990-2012: Marriage of Convenience or Strategic Alliance?*, Routledge, Durham 2014, p. 80.

<sup>89</sup> A. Raval, D. Sheppard, *IEA warns of ever-growing reliance on Middle Eastern oil supplies*, in „Financial Times”, July 7, 2016, see [www.ft.com/cms/s/0/a36bfe6e-4367-11e6-9b66-0712b3873ae1.html](http://www.ft.com/cms/s/0/a36bfe6e-4367-11e6-9b66-0712b3873ae1.html) (accessed on 28 July 2016).

<sup>90</sup> C. R. Mohan, L. Powell, *op. cit.*, p. 146; see T. Madan, *op. cit.*, The James A. Baker III Institute For Public Policy Rice University, 2007, p. 55.

<sup>91</sup> T. Madan, *op. cit.*, The James A. Baker III Institute For Public Policy Rice University, 2007, p. 58.

<sup>92</sup> K. Wysoczańska, *Sino-Indian co-operation in Africa: Joint efforts in the oil sector*, in „Journal of Contemporary African Studies”, vol. 29, no. 2, 2011, p. 196.

oil that they buy abroad passes through choke points. To mitigate this challenge, they strengthen their navies and develop new pipelines. But the small dimension of these pipeline projects mitigates the problems, not solves them. Much more has to be done. The second challenge that they face is their dependence on Middle Eastern oil, especially from Persian Gulf countries. To mitigate this problem, their oil companies invested all over the world to get access to oil fields. Africa, Central Asia, Latin America and Russia – the list of regions where companies from China and India invest seems to be without the end.

Most of these investments were done in a high price environment. They contributed substantially to the global rise of supply. But in mid-2014 prices started to fall and market conditions changed. Production in many areas is uneconomic and the importance of Middle Eastern oil is growing. The IEA sees this as a problem for all oil importers, but it is especially the Asian consumers who are in danger in consequence of their traditional high dependence on Middle Eastern oil.

Energy diplomacy of India and China changed the role of oil companies from these countries on the oil market. Today they are competitors and partners of well established companies from the United States and Western Europe in many projects. Despite their aggressive investment strategy (especially Chinese companies, less so the Indian ones) and governmental support, they have never questioned market principles. China and India appreciate an open and smooth functioning oil market. The emergence of oil companies from China and India in the market strengthened the competition in the market but did not change its principles. Oil companies from China and India are rather active market participants; their strategy better coexists with the strategy of their home governments than instruments of state policy in neo-mercantilist sense.

## **ENERGY SECURITY AND ENERGY DIPLOMACY OF CHINA AND INDIA IN THE 21<sup>st</sup> CENTURY**

*(Abstract)*

The goal of this paper is to analyse the challenges to the energy security of China and India in the 21<sup>st</sup> century and the countries' response in form of energy diplomacy. I will argue that the energy diplomacy of China and India allowed oil companies from both countries to become important players in the market but only indirectly increased the energy security of their home countries. Contrary to the initial concerns, the energy diplomacy of China and India has not changed the structure of the market or challenged the principles of their foreign policy.

*Keywords:* India, China, energy security, energy diplomacy.