ENERGY RESOURCES AND ENERGY POLICY

THE CHINESE DRAGON IS THIRSTY FOR OIL AND GAS

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Twenty-five years ago China (despite its theoretically high annual economic growth rates of 7-8%) was teetering on the brink of hunger strikes and sociopolitical destabilization. The country was in the need of reform, the foundation for which was laid at the December (1978) Plenum of the CPC Central Committee. The reform policy is characterized by extremely careful and unhurried dismantling of the planned-distribution system and its gradual replacement with a market system. However, it is based on the well-known pragmatic maxim coined by Deng Xiaoping: "It doesn't matter what color the cat is as long as it catches mice." This "cat," the so-called "socialist market," has taken root in the local soil and, by successfully "catching mice," has led to the rapid development of the country's economy. In this way, the attempt to create a market economic system by retaining the communist party's monopoly on political power has been crowned with indisputable success. Today, the PRC is a country with a mixed economy, in which the share of the state sector in the GDP does not exceed 40%.

There can be no doubt that long coexistence of two different systems has also given rise to significant losses. But the pluses of the strategy adopted for reforming the economy still outweigh the minuses.

The Growing Economy

The policy of gradual reform led to the country's rapid upswing. From a poor country oriented toward its domestic market, it has become one of the most dynamically developing states, currently holding fifth place in the world in terms of foreign trade volume. Its membership in the World Trade Organization (2001), the inflow of direct foreign investments, and the increase in export have accelerated this growth even more.

During the past three years, the increase in China's GDP amounted to one third of the world economic growth rates (in terms of purchasing power parity), which is twice as high as in the U.S. According to the PRC State Statistics Board, in 2002, the GDP increased by 8%, and in 2003 by 9.1%. Nevertheless, many consider that even these indices do not reflect reality. For example, experts from the leading rating business, Standard & Poor's, note that in reality this growth could reach 11-12%. The International Monetary Fund forecasts that in 2004 it will increase by 8.5%, while analysts from Goldman Sachs quote a figure of 11.8%. What is more, as PRC Chairman Hu Jintao stated recently, by 2020, Beijing hopes to raise its GDP another four-fold.

Over the past 10 years, the export of the Celestial Kingdom increased from 120 billion dollars in 1994 to 438 billion dollars in 2003. And in the next five years, this index will grow by at least another 600 billion dollars, making the PRC the largest exporter in the world. Even today, its commodities have flooded many countries and continents. China is the fourth largest exporter in the world. The bulk of its production goes to the U.S. and Japan, accounting for 1% of the U.S.'s GDP and 1.5% of Japan's. Industrial production accounts for more than 85% of PRC export and primary processing products for about 13%.

In a short time, the country, which used to put out mass consumer goods—toys, footwear, and clothing—has joined the ranks of those states specializing in the manufacture of high-tech and scientific-intensive production. Today, more than 30% of Chinese export comprises electronics, household appliances, and industrial equipment. Many transnational corporations are building or have already built their own enterprises in the PRC. In 2003, the inflow of direct investments into the country reached 53.5 billion dollars. According to the forecasts, approximately the same amount is expected in 2004.

China's share in the world economy today is a little more than 4%, but, in so doing, the country consumes 40% of all the cement produced in the world, 33% of the coal, 27% of the steel, more than 25% of the copper, 19% of the aluminum, and 20% of the nickel. The Celestial Kingdom also accounts for a third of the increase in the world demand for oil, placing it ahead of Japan and only second to the U.S.

In 2003, the PRC's GDP amounted to 11.67 trillion yuan (1.40 trillion dollars), with a foreign trade turnover of 851.2 billion dollars.[1] According to the People's Bank, at the end of March 2004, the country's hard currency reserves were estimated at almost 440 billion dollars (which is four-fold higher than the U.S.'s foreign currency reserves). China today is one of the fastest developing countries in the world. Some analysts presume that by 2005, its economy will reach the level of Japan's,[2] and by 2010, it could even surpass the U.S., although others say this will not happen until 2020.[3] Many experts agree that Beijing will be able to retain its growth rates at 6-7% a year for a long time to come, that is, double its GDP every ten years.

Problems Remain

Despite the enormous achievements, the same economic growth has been creating a multitude of problems in the country in recent years, which are proving very difficult to resolve. The most serious of them are: the acute shortage of transportation, energy, and raw material resources, the weak banking sector, the widespread corruption, and the growing inequality in development between the eastern and western regions, and the cities and villages, as well as in personal incomes.[4] The high, although still latent,

[1] See: *Renmin ribao,* 6 March, 2004.

[2] See: *Financial Times Report on China*, 2 June, 1995.

[3] See: P. Dibb, *Towards a New Balance of Power in Asia. Adelphi Paper 295*, Oxford University Press for the IISS, 1995, p. 27.

[4] According to official data, the highest salary is 245-fold more than the lowest, and when taking into account other income, the difference is twice as high again. In so doing, the 50 richest people in China own a quarter of the entire property in the country, and a tenth of the population owns half of all the bank deposits.

social tension is aggravated by the low efficiency of the social security system, which for most of the country's residents is essentially non-existent.

Unemployment arouses great concern. For example, according to official data, in 1999 and 2000, it amounted to approximately 3.1%, in 2001 to 3.6%, in 2002 to 4%, and in 2003 it could hardly be kept from rising above the 4.5% mark.[5] But independent experts estimate the real unemployment level at 25% of the able-bodied population, which amounts to about 700 million people. At present, the Chinese economy, if its growth rate remains at a level of 7-8%, is capable of creating up to 8 million new jobs a year, but approximately 13 million workers join the labor market annually. And it appears Beijing does not know how to resolve the problem of finding jobs for the slowly burgeoning multi-million army of unemployed within the framework of an economy built on a mixture of market relations and strict administrative regulation.

The structural priorities of the reforms are shifting toward scientific-intensive production units and integration into both the regional and the global economy. But in the near future, the country will have to define the balance between its national and regional economic interests. How can it raise the efficiency of the economy and avoid an abrupt rise in unemployment? To what extent should it increase the presence of foreign capital? How long can the communist party's monopoly be retained on political power under conditions of a market and integrating economy? How can a balance be ensured between market conditions of economic activity and the socialist political system?

Several economists forecast "overheating"[6] of the economy and express doubts that the Chinese miracle can continue to manifest itself. In their opinion, the accumulated investments already threaten the PRC's economic stability, and the current situation is very like the one that preceded the East Asian crisis of 1997.

Residential real estate, ferrous metallurgy, and car-building are resting on quicksand, and power engineering has been stretched to the limits of its capacity. According to the estimates of IMF experts, the economic boom in the Celestial Kingdom is ensured 75% by the inflow of capital, whereas the cumulative productivity factor (the indicator of the economy's overall efficiency) only increased by 2% in 1995-1999.[7] In this respect, not only must the development model be urgently changed, but economic growth must also be reoriented toward using the potential of the domestic nongovernmental economy.

China's Hydrocarbon Resources

It is difficult to obtain real data on the PRC's proven and potential oil supplies, but most experts agree that they constitute approximately 70 billion barrels. Forty billion barrels of this amount are concentrated on dry land and 30 billion barrels are offshore. The latter are distributed approximately as follows: 40% in the East China Sea, and 30% each in the South China and Yellow seas.[8] It should be noted that due to disputes about who owns certain border territories, the potentially rich regions, which the Celestial Kingdom unofficially considers under its jurisdiction, are not included here.

Along with the South China Sea, oil exploration efforts are focused on the Xinjiang-Uighur Autonomous Region. However, the oil produced here has been used mainly for local consumption for more than fifty years now, and there are no major oil pipelines to link the XUAR with the rest of China. According to geologists, 20.9 billion tonnes of oil and more than 1 trillion cubic m of gas are concentrated in Xinjiang, which amounts to 25.5% and 27.9% of their national supplies, respectively. At the

[5] See: [http://www.airi.kz/doclad], 15 October, 2004.

[6] The term "overheating" means extreme financing of economic growth. It happens when investment, consumer and state spending are not carried out evenly, but fall on the same period and, as a rule, are accompanied by immense inflation and devaluation of the national currency. Taking into account the size of the PRC economy, "overheating" could be followed by catastrophic "compression" with a subsequent drop in global demand and a collapse in prices for resources.

[7] See: [http://www.airi.kz/doclad], 15 October, 2004.

[8] See: *China Energy Study, East-West Center*, Honolulu, Hawaii, 1988.

end of 2003, the proven geological supplies of oil in the region were estimated at 2.7 billion tonnes and of gas at 975.3 billion cubic m. In 2003, their total production volume was 21.4 million tonnes and 5 billion cubic m, respectively.[9] In order to raise production efficiency, the Chinese National Petroleum Company (CNPC) formed three subdivisions—the Xinjiang Oilfield Company, the Tarim Oilfield Company, and the Tuha Oilfield Company. They divided the old Jungar Basin (its center is the Karamai field), the Tarim Basin, and the Tuha Basin among themselves, respectively.

In order to develop these resources, investments of more than 15 billion dollars are needed, but the CNPC is unable to independently "raise" the XUAR, especially to a level where its oil becomes one of the foundations of national economic development. Consequently, it has been holding international tenders (since 1994) for the right to carry out oil surveying in this region. But Beijing is disappointed in the results of the work conducted by the foreign companies, Agip, Elf, Texaco, BP, and Esso, since they failed to find any new large supplies. Nevertheless, this did not interrupt the positive trends, and in recent years both production and proven supplies have been growing in the XUAR.

Proven Supplies of Oil by the CNPC in the XUAR (*mill. t*)

Fields	1996	1997	1998	1999	2000	2001	2002
Xinjiang (Jungar)	102.1	108.1	141.5	145.7	148.0	148.5	150.3
Tarim	57	52	47.3	51.5	63.6	67.5	71.2
Tuha	20.6	28.1	26	25	26.8	27.3	28.5
Total	179.7	188.2	214.8	222.2	238.4	243.3	250

Sources: CNPC; PetroChina.

Oil Production by CNPC in the XUAR (*mill. t*)

Fields	1996	1997	1998	1999	2000	2001	2002
Xinjiang (Jungar)	8.4	8.9	8.9	9.2	9.4	9.9	10.3
Tarim	3.1	4.3	3.9	4.3	4.4	4.8	5.1
Tuha	3.1	3.2	3.2	3.2	3.1	2.7	2.7
Total	14.6	16.4	16	16.7	16.9	17.4	18.1

Sources: CNPC; PetroChina.

At present, approximately 80% of the oil produced at more than 60 fields is refined at the oil refineries of the PetroChina Company, located in the XUAR. In 2002, PetroChina's local subsidiaries produced more than 18 million tonnes (11% of the country's total production). In 2003, 21.41 million tonnes of oil and more than 5 billion cubic m of gas were produced in this autonomous region. On the whole, Xinjiang's share in China's total production increased from 5% in 1990 to 12% in 2003.

Despite the fact that Chinese geologists estimate the potential supplies of energy resources in the Jungar, Tarim, and Tuha basins at more than 74 billion barrels of oil and 283 trillion cubic feet of gas,

[9] See: [http://www.xinhuanet.com].

new large deposits have not yet been found. The result is legitimate: in June 2003, a representative of PetroChina announced that the fact no new large oil deposits have been found in Tarim and Tuha makes the economic expediency of investments in these basins dubious. So the company has decided not to increase its investments in exploration work in the XUAR. But this decision may also be explained by the fact that it is much more advantageous at present for the PRC to use its neighbors' resources and save its own deposits for more lucrative times.

The construction of an oil pipeline, which PetroChina plans to finish in 2005, complies with this presupposition (it is enough to look at the production indices in the XUAR). This pipeline is to pass from Karamai via Urumchi and Lanzhou to Luoyang and on to the northeast and southeast of the country. It should be noted that implementation of this project was largely promoted by the West-East gas pipeline,[10] the laying of which (from Lunnan via Lanzhou to Shanghai) is also to be completed in 2005. The Chinese oil and gas corporation intends to lay another two pipelines, which will make it possible to deliver crude oil and petroleum products, respectively, from Karamai to the interior regions of the country through Urumchi. And their construction should be finished in 2005.

A total of 80% of oil is produced on the country's northeast coast (most of the local fields have largely been processed), and offshore sources provide only 3% of the total production. However, the PRC's burgeoning economy is in dire need of oil, since at annual economic growth rates of 8%, 420 million barrels of oil a year are required, while at a 10% growth rate this amount will increase to 450 million. The situation is aggravated by the fact that between 1980 and 2002, production dropped by almost 41%, and consumption increased 1.8-fold.[11] If these trends continue, Chinese economists predict that by 2010 the country will have to import 260 million tonnes of oil.

Export and Import of Crude Oil in 1990-2000 (*mill. brls/day)*

	1990	1991	1992	1993	1994	1995	2000
Export	**0.5**	**0.4**	**0.2**	**—**	**—**	**—**	**—**
Import	**—**	**—**	**—**	**0.2**	**0.9**	**0.3**	**2.1**

Sources: BP, Statistical Review; China Energy Study; OPEC.

In order to satisfy growing domestic needs, Beijing is looking toward essentially all the oil-rich regions of the world: the Middle East, Southeast and Central Asia, and Siberia, but most of the oil is currently delivered on large-tonnage tankers from countries of the Persian Gulf, therefore China needs to diversify its flows. At the moment, its greatest problems in doing this are with Russia. The attempts of Chinese oil and gas companies to participate in tenders to purchase shares in Russia's Onako, Slavneft, and Russia-Petroleum, which is the operator of the Kovyktin gas field, have not been crowned with success. CNPC and YUKOS signed an agreement on the delivery of 700 million tonnes of oil between 2005 and 2030.[12] The cost of the contract is estimated at 150 billion dollars. At present, Russian oil is going to China by rail, and implementation of the mentioned contract largely depends on the Russian government's consent to build a pipeline with a capacity of 30 million tonnes of oil a year, which will have to be laid from the rich fields of East Siberia. But its route has still not been decided: one of the main arguments against this project is that Beijing, after becoming the sole customer of this pipeline, will be able to dictate its delivery conditions to Moscow.

[10] The West-East pipeline, which is 1,467 km in length and has a capacity of 12 billion cubic m of gas a year, passes through ten provinces, cities of central subordination, and autonomous regions. At present, 14,000 km of gas pipelines are functioning in the country with a throughput capacity of 32 billion cubic m a year.

[11] See: T. Brown, "Vzaimnoe pritiazhenie," *Neftegazovaia vertikal,* No. 6, 2004, p. 14.

[12] In 2002, all the Russian petroleum companies exported no more than 22 million tonnes of oil by rail (*Vedomosti*, 17 September, 2003).

What is more, the fate of the main lobbyist of this oil pipeline, the YUKOS Company, is very indefinite, since its main shareholders are under arrest for economic crimes. All of this is inclining Russia toward a project which calls for building a pipeline to its Far Eastern port of Nakhodka, being actively lobbied by the Japanese government, and not to China's Daqing.

As for gas deposits, the PRC Commission on Natural Resources has confirmed 1.37 trillion cubic m of proven and 0.5 trillion cubic m of possible supplies. In particular, the largest field in the country was discovered in 1998 in the Tarim Basin. According to the latest data, its proven supplies already exceed 700 billion cubic m. But, in contrast to oil, 70% of the supplies of blue fuel are in the west of the country and are still not accessible to consumers.

Regional Production and Supplies of Chinese Gas

Region	Production in 1999 (24.3 bill. m^3), %	Supplies as of 1 January, 2000 (1,368 bill. m^3), %
Southwest	36.0	33.5
West	11.0	35.0
Northeast	23.0	7.0
East	13.0	10.5
South China Sea	17.0	14.0

Source: *Neftegazovaia vertikal*, No. 7-8, 2000.

The pipeline network in the PRC is very underdeveloped (its total length is only a little more than 1,700 km), so approximately 70% of petroleum products are delivered by rail, 21% by road, 8% by barges and tankers, and only 1% by pipeline. What is more, there are no national gas pipelines at all, and blue fuel is usually consumed where it is produced. The country is only just starting to build a national gas system, for which there is obviously a great need. Only 30% of gas is produced in the most developed southern and eastern regions of the PRC, where 70% of its GDP is created, whereas in the west and southwest, which provide only 12% of the GDP, 47% is produced.[13]

Annual Per Capita Gas Consumption (m^3)

Country	Volume
China	17
South Korea	400
Japan	600

Source: *Neftegazovaia vertikal*, No. 7-8, 2000.

The government has drawn up a program for increasing gas consumption in the country from the current 24 billion cubic m to 80 billion cubic m by 2010. But since by 2010, its total import will not exceed 25 billion cubic m (only one third of the predicted increase), Beijing is looking at foreign deliveries only as a supplement to its own production. So priority goes to building domestic gas pipelines, which will cross the country in the North-South and West-East directions, keeping in mind the possibility of

[13] See: O. Vinogradova, "Vremia vbivat kolia," *Neftegazovaia vertikal,* No. 7-8, 2000, p. 127.

hooking up to future export pipelines from Russia and Central Asia. But these projects require large amounts of money. The PRC is trying to generate them by placing the shares of its petroleum companies, in particular PetroChina, on the international stock exchanges. But so far these attempts have been rather unsuccessful, since investors were permitted to participate only in construction, and not in corporate management.

Shortage of Energy Resources

Even if it becomes a space nation, in terms of its energy structure, China is still stuck at the beginning of the 20th century and remains a country with a "coal" economy. For example, 75% of the country's main requirements for energy resources are satisfied by coal, 3% by hydropower, 2% by natural gas, and the rest by oil. But the PRC is still experiencing a shortage of energy resources. Since 2003, 2/3 of the Celestial Kingdom has suffered from regular cutbacks in electricity and even its complete cutoff. Building new generating capacities will increase the demand for imported energy resources even more. China is experiencing a growing thirst for oil (at present 6.3 million barrels of oil are consumed a day). In 2003, the increase in its consumption amounted to 11%, and import to 91.12 million tonnes,[14] which is 31% higher than the 2002 index. According to the PRC Ministry of Trade, in 2004, as much as 110 mill. tonnes will be imported.

Whereas Beijing used to orient itself toward ensuring an increase in production at any price in its corresponding development programs, now it is clear that its further extensive increase is impossible. The country's Energy Program for 2004-2020 makes energy saving a top priority for the first time. This will no doubt help to ease the problem somewhat, but an increasingly large amount of energy resources will have to be bought abroad. According to the estimates of the International Energy Agency (IEA), the country is currently importing approximately 2 million barrels of oil a day, whereas domestic production is equal to approximately 3.4 million barrels/day. According to some forecasts, by 2010, import could double, and by 2030, demand will amount to approximately 10 million barrels of foreign oil a day, the amount the U.S. currently imports.[15] IEA experts believe that in the next two years, the PRC will account for one third of the worldwide increase in the demand for oil.

But at present its production in China itself is undergoing many difficulties, and Beijing is feeling a significant shortage of proven deposits. In so doing, the supplies at the old fields have essentially been exhausted. As for the "Chinese Kuwait"—the Tarim Basin, production here is fraught with extremely difficult natural climatic conditions, very complicated geological structures, and high transportation costs, which taken together make the expediency of developing these fields dubious.

The demand for oil is growing so rapidly that not one source in the foreseeable future will be able to satisfy it independently: not one country of the Persian Gulf, nor Kazakhstan, nor Indonesia, nor Russia. So the Chinese are trying to wheedle their way in wherever they can.

In order to satisfy its hydrocarbon needs, Beijing will be required to resolve several major geopolitical, economic, financial, and technical problems, which have been aggravated by territorial disputes. This particularly applies to the South China Sea, where there are large deposits of oil and gas.

The national security strategy China has been carrying out since the beginning of the 1990s envisages "concentrating the main efforts in the eastern and southern vectors, with an emphasis on the north (Russia) and after stabilizing the west (India and Central Asia)." This strategy is explained by the enormous economic significance of these vectors for the Celestial Kingdom: the Chinese Southeast Asia diaspora, which is the largest source of investments, on the one hand, and the rich oil and fish resources of the South China Sea, on the other.

[14] See: [http://russian.xinhuanet.com/htm/04091946382.htm].
[15] See: *Vedomosti*, 4 December, 2003.

The PRC's repeated attempts to resolve territorial disputes by force indicate that its growing demand for oil could give rise to serious regional conflicts. There are more than enough precedents: we only need to recall the conflicts on the Soviet border in 1969, on the island of Daman and in the region of Zhalanashkol Lake (Kazakhstan), as well as the large-scale Sino-Vietnamese war of 1979. A serious build-up of armed forces, particularly naval, will make it possible for Beijing to defend its territorial claims in the oil and gas regions of the South China Sea. For example, China used armed forces to seize the Parasel Islands (1974), and in 1988 and 1991 it again used them to establish control over some of the Spratly Islands, which the Philippines, Taiwan, Vietnam, Malaysia, and Brunei are also making claims to. (In 1993, the Chinese arbitrarily set up their border signs on the archipelago, and in January 1995 carried out the first seizure of territory by building barracks supposedly for its fishermen on Mischief reef, to which the Philippines claims its rights.) The Celestial Kingdom, referring to "historical use" (which is absent in the international practice of maritime law), views the entire archipelago as its own (and we are talking about hundreds of barren islets and cliffs, many of which totally disappear underwater during high tide) with an area of more than 181,000 sq km.

Despite the discouraging results of the exploratory work conducted in the South China Sea in 1980-1984 (out of 120 wells only 39 were oil- and gas-bearing, whereby they contained extractable supplies of less than 100 million barrels), Beijing is sure that the oil supplies in disputed territories around the Spratly Archipelago are comparable to the supplies in Iraq (according to preliminary data—130 billion barrels[16]). And this is why the PRC is insistently trying to make the South China Sea its own interior sea, turning it into a "Chinese lake." After establishing full control over it, the Celestial Kingdom will be able to satisfy its ambitions right up to the territorial waters of neighboring countries, correspondingly obtaining all rights to possible oil and gas fields under the seabed.

China also has such "island" conflicts with Japan (the islands of Senkaku/Diaoyutai) and Taiwan (Beijing denies the latter right to existence at all). In a book which came out at the beginning of 1994 called "China After Deng Xiaoping: Ten Essential Problems," well-known scientists Wu Guoguang and Wang Zhaojun directly raise the question of the "contradiction between the narrow natural base, on the one hand, and the size and growth rates of the population, on the other."

The PRC can resolve these "contradictions" not only by military means, but also by using its favorite strategy of "creeping" attachment: various small enterprises, joint ventures, prestigious companies and banks, hired workers and peasants, "tourists," and so on, fill up the border regions, gradually adjusting not only the market, but also the demographic situation to their own needs. The new foreign policy concept of peaceful revival of the country, "He ping jue qi," officially put forward by the CPC Central Committee in 2003 testifies to the prevalence of this strategy. According to this concept, China, by learning from past lessons, is choosing peace, and by not claiming hegemony, is not threatening other nations. The Chinese revival should guarantee the peaceful and productive development of other countries.[17] There can be no doubt that this will help China to acquire the respectable image of a partner in most states of the world, and not be viewed as a potential enemy.

The Chinese Vector of Kazakhstani Oil

Keeping in mind Astana's ambition plans to become one of the largest world oil producers in the next decade (by 2015, it plans to increase oil production three-fold, that is, to 150 million tonnes), the PRC petroleum market is very attractive to Kazakhstan. Its volume in 2003 was estimated at 1 trillion

[16] See: M. Leifer, "Chinese Economic Reform and Security Policy: The South China Sea Connection," *Survival*, Vol. 37, No. 2, Summer 1995, p. 44.

[17] See: "Premier of the State Council Wei Jiabao at a Press Conference for Chinese and Foreign Journalists," *Renmin ribao,* 15 March, 2004.

dollars.[18] In light of the acute shortage of energy resources the Celestial Kingdom is experiencing, Kazakhstani hydrocarbons are extremely apropos.

The CNPC came to Kazakhstan as early as 1997 and won a tender held at that time, thus obtaining more than 60% of the shares of AO AktobeMunaiGas (AMG) only because it offered Kazakhstan the most attractive set of obligations. One being a proposal to build an oil pipeline to China and a section of the pipeline to the border with Turkmenistan (the Iranian project). What is more, the CNPC was to provide the initial investments in a project for rehabilitating Uzen, but nothing came of all the promises. As a result, it was the Kazakhoil Company that began restoring Uzen, and the question of the Great Chinese Pipeline was essentially removed from the agenda. But most important, CNPC simply did not carry out the investment program it offered AMG, which sold it its shares. Whereas in 1998, this project was carried out by 85.4%, the next year it was only fulfilled by 59.6%, since instead of the 117.4 million dollars envisaged in the contract, only 70 million dollars were allotted. As a result, all the CNPC's activity in Kazakhstan was limited to developing the Zhanazhol and Kenkiyak fields, as well as exporting some of the hydrocarbons Kazakhstan produced by rail.

Nevertheless, over time, China was able to reinforce its foothold in Kazakhstan. In August 2003, the CNPC bought up 35% of the shares of the Northern Buzachi oil and gas fields, then purchased a set belonging to Chevron Texaco. And today the CNPC-AktobeMunaiGas company annually produces approximately 5 million tonnes of oil. And the Chinese Sinopec Corporation has a 50% share in large sections of the Tengiz field.[19] In this way, building a pipeline to China is becoming (politically and economically) one of the highest priority tasks in the development of Kazakhstan's oil and gas industry.

In 2003, the first line of the major oil pipeline to the PRC-Atyrau-Kenkiyak—was put into operation (in the northwest of Kazakhstan). And during Kazakhstan President Nursultan Nazarbaev's visit to the PRC in May 2004, KazTransOil, Kazakhstan's state company on the transportation of oil, and the Chinese National Corporation for Oil Exploration and Development officially signed an agreement on its construction. A few months later on 28 September, a ceremony was held to officially open its construction. In order to implement the project, a joint company, Kazakhstan-Chinese Pipeline, has been created, the founders of which are the above-mentioned KazTransOil Company and the Chinese National Corporation for Oil and Gas Exploration and Development with equal shares.

Reference: The oil pipeline (with a pipe diameter of 813 mm) will join the Atasu oil-pumping station in the Karaganda Region (Kazakhstan) to the railroad station of Alashankou in China. The length is 988 km, throughput capacity at the first stage of the project (2006) is 10m tonnes a year, at the second (2011), up to 20m tonnes, projected cost of the work—700 million dollars, 100 million of which are authorized capital and 600 million borrowed funds. An agreement on cooperation in the oil and gas industry between the governments of China and Kazakhstan defines the financing scheme for construction of the oil pipeline as 50/50. In so doing, 60% of the construction of the linear pipeline will be carried out by Kazakhstani contractors.

The important linear part of the oil pipeline from western Kazakhstan to the western regions of China will be the Atasu-Alashankou section, the total length of which exceeds 3,000 km. After construction is complete, this route will be the first to export Kazakhstani oil without passing through Russian territory. By the way, the possibility is envisaged of pumping Russian oil through this pipeline as well (a proposal to hook up the branch being built for its transportation was made quite a while ago). As Russian Minister of Industry and Energy V. Khristenko noted, the final decision on this question will depend on the operating conditions of this route. In particular, Transneft, which will have to deliver Russian oil to Kazakh-

[18] See: *Vedomosti,* 4 December, 2003.

[19] See: E. Grebenshchikov, "Rossiia-Kitai na perekrestkakh aziatskoi diplomatii," *Aziia i Afrika segodnia*, No. 9, 2004, p. 10.

stan, stated: "We still do not know the parameters of the project, including the tariff Kazakhstan intends to levy." Nevertheless, reference to "operating" makes it possible to assume that the "conditions" might include not only economic, but also political aspects.

At present, the export of Kazakhstani oil to China is much lower than the anticipated capacity of the pipeline being built even at the first stage of its operation. But as Russian Minister of Energy and Mineral Resources V. Shkolnik stated,[20] in compliance with the signed documents regulating the implementation of the project, "the Chinese side is responsible for filling the pipeline." It is presumed that at the first stage, this pipeline will be filled with oil from the South-Turgai fields of Kazakhstan and Russian supplies from West Siberia. It is obvious that hopes are being placed (taking into account the complicated situation with the prospects of the Angarsk-Daqing pipeline in the Russian Far East) on Beijing being able to come to an agreement with Moscow about delivery (at least for the next few years) of the necessary volumes of oil to be transited through Kazakhstan via this route.

In so doing, if this oil pipeline goes into operation, China will reduce is energy dependence on the Arab countries (Oman, Yemen, Iran, and Saudi Arabia are currently covering almost 60% of the oil imported to the Celestial Kingdom). And Kazakhstan, which is planning to raise its hydrocarbon production, for which it will have to create a technically reliable and economically efficient infrastructure for making deliveries to the international markets, "will cut itself a window to the world." What is more, implementation of the "Chinese" pipeline project could change the vector of development in Kazakhstan's export strategy. Instead of the western vector, the eastern will most likely move to the forefront, at least in the political respect, which could have a great impact on the fate of oil projects throughout the entire Caspian Region.

But despite all the attractiveness of the idea of a Great Chinese Pipeline for pumping Kazakhstani oil, there are a multitude of economic, technological, and other obstacles hindering its implementation. For example, the enormous length of the pipeline, the low quality of western Kazakhstani oil (which requires heating during transportation), the absence of an infrastructure, the mountain relief, and the high seismic-risk zones will significantly hike the cost of the project. What is more, a route of this length and with huge investments will only pay for itself if no less than 20 million tonnes of oil a year are pumped along it. And this is only possible if oil production is significantly raised in Western and Central Kazakhstan. At present, our republic is producing a total of a little more than 50 million tonnes (in 2003, 51.2 million tonnes were produced). Of this amount, approximately 9 million tonnes are consumed on the domestic market. The rest go to export, but this export is tightly "attached" to the traditional markets, often via offshore zones, against which it is even difficult for state interests to fight. What is more, if such large amounts of oil go to the East (taking into account the sensitivity of the oil market), the price of oil in Europe will go up. So it is very doubtful that western companies producing oil in Kazakhstan will agree to reorient deliveries to China and fill this pipeline.

The shelf fields of the Caspian could make up the deficit. But their development, assuming enough oil is found, is a long-term prospect. So the Chinese project will most likely repeat the fate of most oil plans in the Caspian Region, where the main thing is not so much oil, as divvying up the sphere of influence, and oil acts only as a tool for resolving geopolitical problems.

Nevertheless, the route to the PRC is creating an alternative to exporting oil to Europe and has competitive advantages compared with its transportation to the West, which involves immense outlays. What is more, implementation of the conceived projects for developing the domestic infrastructure of the Celestial Kingdom will create a potentially vast oil and gas market in this part of Asia. And for Kazakhstan, the economy of which depends on the export of energy resources, it is important not only to retain its position on the traditional European markets, but also gain access to new and promising segments in other regions.

[20] See: *Kursiv,* 30 September, 2004.