The regional and global geopolitics of Russo-Chinese crude oil transport

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Introduction

At a presidential summit in late May 2003, Chinese President Hu Jintao and Russian President Vladimir Putin signed a document declaring Sino-Russian energy cooperation, with China playing the role of customer and Russia the role of vendor, to be a top priority in the bilateral relationship between the two Asian giants.[1] Given that said agreement seemed to reaffirm and strengthen the "strategic partnership" to which the two countries committed in July 2001, and that it occurred in the immediate wake of the globally-reviled invasion of Iraq led by the United States, it appeared to mark an event of momentous geopolitical significance, not only at the Northeast Asian but also the world level. Another intimately related milestone was reached at some undefined point in the same year. In January 2004, the International Energy Agency (IEA) announced that in 2003 China passed Japan to become the second-largest crude oil-consuming economy on the planet, its ravenous appetite driven by its booming industrial export sector and the hothouse "automobilization" of its urban transport rolling stock.[2] Moreover, in 2003 more than one-third of China's teeming demand for crude oil was sourced abroad, with dramatically rising import dependence forecast decade-on-decade into the future.[3] Especially considering how radically increasing political volatility in and around Iraq threatens to interrupt the predictable flow of low-cost crude oil from the Persian Gulf (currently supplying about half of China's import total) to East Asia, China's rapidly growing thirst for hydrocarbon fuels should only reinforce Sino-Russian energy cooperation and hence Sino-Russian "strategic partnership" in the 21st Century – or will it?

[1] Page, Jeremy, "Russia, China to step up oil cooperation," Reuters wire service, May 27, 2003.
[2] Mallet, Victor, "China unable to quench thirst for oil," *Financial Times*, January 21, 2004.
[3] Mallet, *op. cit.*.

Hu and Putin's declaration ostensibly gave official blessing to a less ballyhooed energy cooperation endeavor long in the works between Chinese state enterprise crude oil refiners and Russian private capitalist crude oil extractors – but this was less a binding compact than a diplomatic nicety, as we shall see. The late May 2003 summit provided a stage for China's National Petroleum Company (CNPC) and Russia's now embattled Yukos (Corporation) to finalize a preliminary agreement that had been several years in the making.[4] Per the terms of the deal, beginning in 2005 and proceeding until roughly 2030 Yukos promised to ship about 5 billion barrels of oil to CNPC facilities in northeast China.[5] The oil was to be transported in a yet to be built 2400-km pipeline connecting Angarsk in eastern Siberia to the famed Chinese petroleum complex of Daqing in Heilongjiang Province. According to the agreement, Russia's public sector oil pipeline monopoly, Transneft, would put up the money to cover the construction cost of the Russian leg of the pipeline (estimated at U.S. $1.8 billion) and would also retain ownership rights over said portion.[6] However, after almost a year of stalling and deliberation on the part of the Kremlin, it was all but clear that Russia would renege on what had earlier looked like a virtual grant of approval for the Angarsk-Daqing pipeline. In late March 2004 Transneft proclaimed that it would instead build a significantly longer (3900 km) and significantly more expensive ($10 million) pipeline running from Angarsk to the port city of Nakhodka on Russia's Sea of Japan coast (although it was not entirely

[4] "Pipeline will move Siberian crude oil to China," *Oil and Gas Journal*, June 12, 2000, p. 75.
[5] Isachenkov, Vladimir, "China, Russia issue multipolar world call," Associated Press wire service, May 28, 2003.
[6] Helmer, John, "Kremlin decides Russia pipeline on new terms," *Asia Times Online*, March 4, 2003 http://www.atimes.com/atimes/Central_Asia/EC04Ag01.html.

clear whether it would definitely abandon a pipeline to Daqing altogether).[7] Consistent with this scheme, supertankers docking at the bulk depots of Nakhodka will ferry crude oil to multiple Pacific Rim clients, especially but not exclusively Japan. Beijing and the CNPC were soothed with assurances that at some unspecified date a Daqing branch pipeline hooked into the Angarsk-Nakhodka trunk pipeline might be built.[8] Nonetheless, all parties implicitly understand that a trunk pipeline all the way from Angarsk to Nakhodka will not carry enough crude oil volume for the foreseeable future to warrant the building of such a Daqing branch pipeline, if ever.[9]

After reviewing the saga of the Angarsk pipeline in more fine-grained detail, in this paper I pose, and at least begin to answer, the two following questions. One, does Russia's reversal on the initial CNPC-Yukos proposal represent the effective scotching of much-acclaimed Sino-Russian energy cooperation? Two, and more gravely, does this reversal also signal the perhaps fatal weakening of the Sino-Russian "strategic partnership," with all of its heady global implications – most importantly, the way in which Sino-Russian solidarity and coordination in international affairs bolsters China's effort to make its deepening integration into the capitalist world-economy work on its own terms, rather than those of the G7 countries (especially the U.S.), their transnational corporations (especially the Fortune 500), and their *rentier* institutions (especially those located on Wall Street)? In response to the first question, I argue that Moscow has settled

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[7] Blagov, Sergei, "Russia hails partnership with Beijing … sort of," *Asia Times Online*, March 25, 2004 http://www.atimes.com/atimes/Central_Asia/FC25Ag01.html; McGregor, Richard, Arkady Ostrovsky, and David Pilling, "Japan expects to win pipeline route," *Financial Times*, March 24, 2004.
[8] Blagov, *op. cit.*.
[9] Blagov, Sergei, "Putin to expand strategic partnership with China," *Asia Times Online*, March 12, 2004 http://www.atimes.com/atimes/Central_Asia/FC12Ag01.html.

in favor of the Angarsk-Nakhodka pipeline rather than the Angarsk-Daqing pipeline for two essential and intertwined reasons, neither of which translates into a decisive turn away from Sino-Russian energy cooperation. One, the Kremlin's forsaking of the pipeline to Daqing for the time being is part and parcel of its clipping the wings of Yukos, itself part and parcel of a broader and decidedly laudable strategy to adjust Russia's development (or "underdevelopment") model so that it no longer brazenly permits the notorious "oligarchs" to cash out their ill-begotten natural resource concessions, but instead deploys natural resource export earnings in the service of reviving decrepit domestic industry.

Two, from the pragmatic perspective of crude oil export economics, the Nakhodka pipeline is actually the sounder and less risky investment option. This is the case for several reasons. One, a Japanese government development bank has offered to extend Transneft a soft loan to cover the complete construction cost of the pipeline. Two, the same development bank has also offered the Russian state and Russian crude oil exporters additional concessionary funding dedicated to the development of unexploited and undiscovered petroleum fields in eastern Siberia, near Lake Baikal. And three, a pipeline terminating on the Sea of Japan would permit Russian crude oil producers to access a diverse array of purchasers, allocating output to each in accordance with shifting market conditions, rather than a single purchaser (the CNPC) that pays a predetermined and thus conceivably sub-optimal price. While Moscow's choosing of the Nakhodka rather than the Daqing pipeline may objectively cause hard feelings in Beijing, then, it does not indicate any kind of overarching retreat from a long-term commitment to Sino-Russian energy cooperation.

Moreover, in response to the second question, I argue that to the minimal extent that the Kremlin's ruling on the Angarsk pipeline signifies any kind of setback at all for Sino-Russian energy cooperation, its effect on the broader pattern of Sino-Russian "strategic partnership," which continually proceeds in a series of graduated steps, is negligible. I tentatively make the argument that a collection of several far-flung but interrelated processes – 1) the secular plunge of the dollar *vis a vis* the euro, 2) Putin's portentous musings about Russia denominating its crude oil export sales in euros rather than dollars, 3) the exponentially flagging capacity of U.S. military prowess to ensure a predictable flow of low-cost Persian Gulf crude oil to the world market, and 4) the Chinese Communist Party's (CCP's) recent drift, however subtle, toward an accumulation regime oriented more toward meeting internal social and environmental needs rather than the external cost-cutting and speculative imperatives of First World (especially U.S.) finance capital – will almost necessitate that China deepen the "strategic partnership" with its vast neighbor to the north if it wants to successfully prosecute its goals of broad-based domestic growth and national security, however much it may now feel aggrieved by the Kremlin's very disappointing decision on the Angarsk pipeline. Indeed, as I will show, a hodgepodge of individually small but collectively large Sino-Russian projects in the Northeast China-Russian Far East (RFE) border zone, some of which directly deal with energy cooperation, illustrate incipient tendencies toward "strategic partnership" being meaningfully expressed in the form of geo-economic integration between the two states.

Crude oil demand and supply conditions in Northeast Asia

Despite not becoming a net importer of petroleum until 1993, as of early 2003, China was the world's third largest net importer of crude oil, lagging behind only the U.S. and Japan.[10] According to the IEA, at some point in 2004 China will surpass Japan as the world's second largest net importer of petroleum.[11] At the beginning of the third millennium, 31 percent of China's overall crude oil consumption was supplied from outside the country; what with the most recent year-on-year increase in China's net crude oil imports registering at a breathtaking 31 percent, some petroleum industry analysts and traders are now projecting that by 2030 upwards of three-quarters of China's total crude oil needs will be sourced abroad.[12] What is generating such monstrous annual growth in China's volume of net crude oil imports and subjecting it to more and more profound dependence on foreign sources of crude oil? To oversimplify, in the last couple of years China's economy (or at least that of China's metropolitan littoral) confidently turned the corner into energy-intensive Rostowian take-off, while at the same time its domestic crude oil output flatlined. China's newly minted "red capitalists" and professional-technical strata bought 69 percent more petroleum-fueled automobiles in 2003 than in

[10] "The Great Game in the Far East," *Transitions Online*, June 2, 2003; Blagov, Sergei, "Russia eyes new oil markets in Asia-Pacific," *Asia Times Online*, April 2, 2003 http://www.atimes.com/atimes/Central_Asia/ED02Ag02.html.
[11] "China to increase oil-supply security," *People's Daily Online*, January 9, 2004.
[12] "China to face challenges in energy in next 20 years," *People's Daily Online*, December 16, 2003; Wonacott, Peter, Jeane Whalen, and Bushee Bahree, "China's growing thirst for oil remakes world market," *Wall Street Journal*, December 3, 2003; Mallet, *op. cit.*.

2002.[13] Even though at the latest National People's Congress the CCP stated its genuine intent to ramp up mass transit investment to stem runaway "automobilization," the party-state's own think-tanks believe that China's private car fleet will quintuple in the next decade.[14] China's consumption of primary energy-generated electricity has leapt by more than 10 percent annually since 1998.[15] Meanwhile, China's aboriginal endowment of crude oil, never generous to begin with (especially when compared to the immensity of its human population), is being progressively sucked dry. The petroleum fields of Daqing, once a legendary monument to socialist self-reliance in the heyday of Maoist development, are in irreversible decline: in 2003, their output dipped below the 50 million ton threshold for the first time since 1975.[16] China's per capita crude oil reserves have shriveled to a puny 11.1 percent of the world average, and some experts have corrected even this dismal statistic downwards.[17]

At present, roughly 60 percent of China's petroleum imports come from those states of the Middle East that straddle the Persian Gulf, by far and away the earth's most bountiful reservoir of proven crude oil reserves.[18] More than three-quarters of that 60 percent comes from Saudi Arabia, Iran, and Oman, in descending order.[19] If one extrapolates from current trends, China will continue to become more and more dependent upon Persian Gulf crude oil to meet its burgeoning domestic needs. If these

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[13] Luft, Gal, and Anne Korin, "The Sino-Saudi connection," *Commentary*, March 2004.
[14] Wonacott *et. al.*, *op. cit.*.
[15] Goodman, Peter, "China's dark days and darker nights," *Washington Post*, January 5, 2004.
[16] "China suspends crude oil exports to Japan," *People's Daily Online*, February 21, 2004.
[17] "China to face energy challenges," *op. cit.*; Nandakumar J, "Energy politics and China's future," *Asia Times Online*, Mar 10, 2004 http://www.atimes.com/atimes/China/FC10Ad04.html.
[18] Luft, Gal, "U.S., China are in collision course over oil," *Los Angeles Times*, February 2, 2004.
[19] Luft and Korin, *op. cit.*; Lelyveld, Michael, "Russia tests China's patience over pipeline," *Asia Times Online*, February 28, 2003 http://www.atimes.com/atimes/Central_Asia/EB28Ag01.html.

trends persist, by 2010 the Middle East will supply more than three-quarters of China's crude oil imports.[20] Yet there are a host of factors that call into question whether China will indeed come to rely so heavily upon the Persian Gulf as its chief source of imported petroleum, at least to the extent the aforementioned forecast suggests. Drastic growth of China's crude oil imports from the Middle East may not reach expected targets for several inextricably tied reasons. One, the botched military occupation of Iraq, degenerating week by week, will immeasurably delay the rehabilitation of its battered crude oil extraction infrastructure and the release of sizable flows of its cheap petroleum onto the world market, as well as amplify the chances of political unrest in neighboring states that export crude oil, most notably Saudi Arabia and Iran.[21] Given that China accesses much more petroleum from Saudi Arabia and Iran than Iraq, region-wide pan-Arabic and/or pan-Islamic revolts from below seem to pose a much more serious challenge to China's soaring Middle Eastern crude oil dependency than does the ongoing stagnation of insurgent Iraq's petroleum export sector. But the ineluctable fact that no "Iraq bonanza" is forthcoming any time soon does impact China's projected super-dependence on crude oil extracted in and around the Persian Gulf. By contributing to an emerging global petroleum bottleneck that is progressively pushing up real world market prices to a level unseen in the "cheap oil" years of 1986-1999, the continued idling of Iraq's crude oil export capacity will bring onstream petroleum exploration and development projects in remote, formerly unprofitable locales, including Russia east of the Urals, geographically proximate to China.

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[20] "Fueling China's Growth," *New York Times*, December 24, 2000.
[21] McKillop, Andrew, "Bush-Blair-Aznar oil war in Iraq was 'illegal, immoral and unjust,'" *Vheadline.com*, March 15, 2004 http://www.vheadline.com/readnews.asp?id=16380.

Two, reports are starting to leak from ARAMCO, Saudi Arabia's parastatal petroleum firm, that the humongous crude oil field (in the words of one journalist) "undergirding Saudi output" is suffering from an unanticipated acceleration of saltwater intrusion and hence an unanticipated acceleration of productivity loss.[22] In less and less hushed tones industry insiders are now remarking that because Ghawar, the mega-petroleum field that currently accounts for more than half of Saudi Arabia's total crude oil output, is showing surprisingly early signs of irrevocable exhaustion, ARAMCO could conceivably fall short of its projected 2011 production goals by some 4 or 5 million barrels of petroleum per day.[23] The premature decay of Saudi Arabia's heretofore bellwether crude oil field will only expedite the upward march of real petroleum prices in the world market, adding momentum to the viable commercial development of Russia's east Siberian and Far Eastern crude oil deposits in China's (if not the world's) backyard. Three, the concatenation of the Middle East in intensifying disarray, the Iraqi petroleum export infrastructure stalled in disrepair, and the gathering cloud over the Saudi Arabian petroleum industry is occurring in the context of booming crude oil demand in the large-market countries of the Global South, not only China, but also India, Brazil, and the like. For example, in the late 1990's and early 2000's, India's inventory of vehicles outfitted with internal combustion engines was growing at an even faster rate than China's.[24] The increasing petroleum thirst of the demographically weighty states in the non-rich world (led by China) allowed the Organization of Petroleum Exporting Countries (OPEC) and

[22] Gerth, Jeff, "Forecast of rising oil demand challenges tired Saudi fields," *New York Times*, February 24, 2004.
[23] Gerth, *op. cit.*.
[24] McKillop, Andrew, "Whatever happened to bargain basement oil?" *Vheadline.com*, March 21, 2004 http://www.vheadline.com/readnews.asp?id=16458.

other crude oil-exporting states to elevate the world market price of petroleum at well above $30 a barrel throughout 2003, with the price only moving higher thus far in 2004.[25]

This upward pressure on the world market price of crude oil is and will continue to be compounded by a largely hidden but terribly critical fact: no new discoveries of a single petroleum field containing at least 5 billion barrels has been made since 1964, and at about the same time the rate of growth of global crude oil reserves began to interminably slow.[26] ARAMCO's second top executive claims that in a mere 6 years an astonishing 50 percent of world fossil fuel consumption will have to met by fields and reservoirs that are untapped as of yet.[27] This bundle of parallel developments points to the conclusion that the lifting of petroleum from the distant fields of Asian Russia, including those plugged into the Angarsk pipeline, will increasingly offer a decent rate on investment to producers and their financiers. This in turn points to the conclusion that, despite the forecasts of China's arithmetically growing dependence on crude oil sourced from the Persian Gulf, China (and other Northeast Asian countries) will come to lean more heavily on the fossil fuel energy supplies of Siberia and the Russian Far East.[28] For their part, Russian state energy planners intend to augment crude oil output by some 1.5 million barrels per day by the end of the decade, and also to spread the number of

[25] Wonacott *et. al.*, *op. cit.*.

[26] McKillop, "Whatever happened to bargain basement oil?" *op. cit.*.

[27] Gerth, *op. cit.*.

[28] Bremmer, Ian and Clark, Bruce, "The Other Great Game," *Moscow Times*, May 12, 2003. In this paper I do not examine one reason why China's dependence on petroleum imported from the Persian Gulf might indeed escalate to the extent that conventional forecasts suggest – Beijing's clever arms transfers and diplomatic overtures to a Saudi Arabia now in the figurative if not literal gunsights of U.S. neo-cons and hawks looking to take the "war on terror" to Riyadh. See Luft and Korin, *op. cit.*; McKillop, "Whatever happened to bargain basement oil?" *op. cit.*; Wonacott *et. al.*, *op. cit.*. It is beyond the modesty of this observer to predict what kind of reaction a full-blown "strategic partnership" between China and Saudi Arabia would elicit from Washington, *i.e.*, whether or not an attempt on the part of Beijing to forge a privileged relationship with Saudi Arabia would backfire and at the end of the day trigger a reduction in China's relative reliance on crude oil imported from the Persian Gulf.

markets to which their hydrocarbon exports are destined.[29] A pivotal element of this approach is the cultivation of new petroleum clients in the Asia-Pacific region, including China. According to the Kremlin's scheme for energy sector development, the so-called "Main Provisions of the Russian Energy Strategy to 2020" adopted in late May 2003, by 2020 Russian crude oil exports to the Asia-Pacific region could well constitute one-third of Russia's total petroleum exports, topping 2 million barrels per year.[30]

The tortuous saga of the Angarsk petroleum pipeline

In late May 2003, Yukos and the CNPC inked a preliminary agreement in which Yukos promised CNPC delivery of 5 billion barrels of crude oil over a 25-year period starting in 2005. The agreement stipulated that the petroleum would be transported in a 2400-km pipeline, yet to be built, connecting Angarsk in eastern Siberia to Daqing in Northeast China's Heilongjiang Province. Transneft would fund the Russian arm of the pipeline (estimated at U.S. $1.8 billion) and claim ownership rights over said portion of the pipeline.[31] Prior to tentatively vetting the Yukos-CNPC deal, the Kremlin had for many months given strong consideration to a rival proposal that would have directed the pipeline from Angarsk to a Russian port on the Sea of Japan, most likely within the municipality of Nakhodka.[32] The Japanese central government, seeking to ease its dependence on petroleum imported from the ever more volatile Middle East, and concomitantly its dependence on the fragile U.S. military superstructure draped over the Middle East, had backed this proposal. Indeed, a Japanese state development bank had

[29] Helmer, John, "A tale of two asses – what will Kasyanov do on the China road?" *The Russia Journal*, September 25, 2003.
[30] Ivanov, Vladimir, "Russia emerging as energy powerhouse," *Daily Yomiuri*, June 13, 2003.
[31] Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*.
[32] Isachenkov, *op. cit.*.

gone so far as to offer to finance the complete cost of an exorbitantly expensive ($5 billion, later to mushroom to $10 billion) 3800-km Angarsk-Nakhodka pipeline with a low-interest loan.[33] So why, in the immediate aftermath of the Sino-Russian presidential summit in late May 2003, did the Kremlin appear to be leaning toward giving its final approval to the Angarsk-Daqing pipeline rather than the Angarsk-Nakhodka option?

First, in exchange for the generous financing it dangled in front of the Kremlin, Japan wanted a guarantee that it would be the exclusive receiver of all crude oil transiting through the Angarsk-Nakhodka pipeline.[34] When negotiations prompted Japan to shade away from this maximalist demand, it insisted at the very least that in return for its financing it be guaranteed exclusive delivery of pipeline petroleum until the loan was fully amortized by Russia's petroleum export revenues.[35] Such a hardball position on Japan's part essentially defeated one of the most appealing aspects of the Angarsk-Nakhodka pipeline alternative from the Kremlin's point of view, namely that crude oil from a pipeline terminating on Russia's Far Eastern coast could be exported to a diverse array of customers – not only Japan, but also South Korea, China, and the U.S., among others.

Second is a hypothetical explanation that received support in certain published news articles appearing in the Western press, but was not universally shared by all of those who had an informed opinion on the matter. A number of years ago, when Yukos

[33] Brooke, James, "Russia's latest oil and gas oasis," *New York Times*, May 13, 2003; Ivanov, *op. cit.*; Lelyveld, Michael, "Moscow clears way for pipeline to China," *Asia Times Online*, May 3, 2003 http://www.atimes.com/atimes/Central_Asia/EE03Ag02.html.
[34] Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*.
[35] Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*.

and CNPC began to mutually explore the concept of an Angarsk-Daqing pipeline, Yukos presumed that it would underwrite the construction of the pipeline, own it, and collect fees from the passage of crude oil through it. However, after Yukos and CNPC launched these exploratory talks several years ago, Putin's Kremlin and Energy Ministry took a more aggressive stand against huge private sector conglomerates (*i.e.*, "oligarchs") reaping super-profits from cheaply selling off Russia's natural resource wealth, and in relation to this became bent on restraining Yukos' ability to exercise such preponderant influence over Russia's petroleum exporting practices.[36] According to this line of interpretation, in public the Kremlin and the Energy Ministry entertained the Angarsk-Nakhodka pipeline option mainly in order to bring Yukos to heel and to strengthen the state power's interest in shaping the terms under which a Angarsk-Daqing pipeline deal would be done, not because it was genuinely serious about lending final approval to such an option.[37] As it turned out by the late spring of 2003, Yukos had been forced to capitulate to Moscow's preference: were the Daqing pipeline to be actually built, Yukos would be reduced to a simple supplier of crude oil to CNPC, rather than a multi-purpose financer of the project, owner of the pipeline, and collector of petroleum transit levies.[38] At least at the time, Moscow's tentative embrace of the Daqing pipeline in late spring 2003 quieted speculation that the Kremlin was opposed to such a pipeline because it did not want a single customer (the CNPC) or a single country (China) to monopolize the offtake.[39]

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[36] Latynina, Yulia, "A national energy plan fit for Caligula," *Moscow Times*, May 28, 2003; Menshikov, Stanislav, "Coup d'etat in Russia: Fantasy or real danger?" *Moscow Tribune*, June 6, 2003; Weir, Fred, "In Russia, a 'creeping coup?'" *Christian Science Monitor*, June 18, 2003.
[37] Latynina, *op. cit.*; Lelyveld, "Moscow clears way for pipeline to China," *op. cit.*; Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*.
[38] Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*.
[39] Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*.

Third, a number of independent petroleum geologists estimated that eastern Siberia's currently exploitable oil reserves were not sufficient to cover the extreme cost of constructing a very long Angarsk-Nakhodka pipeline over very harsh terrain. In order for Russia to pay off even a below market-rate loan tendered by a Japanese state development bank, 50 million tons of crude oil per year would have to flow from the eastern Siberian crude oil fields to a depot on the Sea of Japan.[40] Hard facts soberly proffered by these petroleum geologists suggested that this would probably be a physical and hence an economic impossibility – unless new crude oil fields in eastern Siberia, both those undiscovered and those discovered but not yet exploited, were brought into production.[41]

The worm turned during July 2003 summit meetings between Russian Deputy Prime Minister Khristenko and Japanese foreign minister Kawaguchi. Japan rescued the viability of an Angasrk-Nakhodka pipeline by offering to finance crude oil field exploration and development in eastern Siberia, a scheme that hypothetically would eventually allow eastern Siberia to yield the oil necessary to make the pipeline economically feasible.[42] Kawaguchi also apparently floated the possibility that Japan would liberalize the conditions attached to the soft loan package, by no longer insisting that all petroleum carried by a pipeline terminating on the shores of the Sea of Japan be

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[40] Blagov, "Russia eyes new oil markets in Asia-Pacific," *op. cit.*; Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*.

[41] Helmer, "Kremlin decides Russia pipeline on new terms," *op. cit.*; Lelyveld, "Moscow clears way for pipeline to China," *op. cit.*.

[42] Ferguson, Joseph, "Partnership or Competition?" *Comparative Connections*, July 2003 http://www.csis.org/pacfor/cc/0302Q.pdf; Helmer, John, "Japan intensifies lobbying for Russian oil," *Asia Times Online*, July 2, 2003 http://www.atimes.com/atimes/Central_Asia/EG03Ag02.html

exclusively bound for the Japanese market until pipeline construction costs were amortized.[43] Russian newspaper articles appearing at the time hinted that Japan was furthermore prepared to cajole the Kremlin into approving the Angarsk-Nakhodka pipeline by extending direct investment in the hydrocarbon sector of the Russian Far East (not eastern Siberia), more particularly by upgrading plant and equipment in the region's petrochemical sector.[44] In essence, this proposition would entail Russia accepting that a big chunk of its crude oil in eastern Siberia would be exported to Japan without any value added, and Japan accepting that a small chunk of the oil it helps transport from Angarsk across the frontier of Asian Russia would have value added to it before it reaches Japanese markets.

Through the autumn of 2003, Russia put off its ultimate decision on the Angarsk pipeline, using stalling tactics to coax further concessions from Japan and possibly hoping as a result that an increasingly anxious CNPC and Chinese central government would voluntarily propose to alter the May 2003 memorandum of understanding on terms favorable to the Kremlin. While Russia played the waiting game, Japan reiterated its $2 billion commitment to help develop the eastern Siberian crude oil fields, and firmly guaranteed that it would no longer require that petroleum delivered through an Angarsk-Nakhodka pipeline be exclusively bound for the Japanese market until pipeline construction costs were paid down.[45] These twin concessions answered two of Russia's

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[43] Helmer, "Japan intensifies lobbying for Russian oil," *op. cit.*.
[44] Ivanov, *op. cit.*.
[45] Brooke, James, "Japan and China battle for Russia's oil and gas," *New York Times*, January 3, 2004;

strongest reservations to the Nakhodka pipeline as previously conceived – that the crude oil fields are not nearly well-developed enough to yield an amount of petroleum sufficient to amortize the considerable expense of a 3800-km pipeline all the way to the shores of the Russian Far East, and that petroleum exports introduced to the world market by a Nakhodka pipeline would not be made immediately available to a wide range of Asia-Pacific consumers. Japan also augmented the appeal of its new position to Russia by affirming that it would not make its participation in a pipeline project contingent upon progress in any other arena of bilateral concern, namely the standing territorial dispute over the Kurile Islands.[46] By late March 2004, although the Kremlin had stopped short of making a formal announcement, comments coming forth from both the Russian Energy Ministry and Transneft made it almost entirely certain that the trunk line of the Angarsk pipeline will be extended to the port of Vostochny, just a few miles up the coast from Nakhodka in Russia's Far East, rather than Daqing.[47] If any further proof were needed, it was reported that Japan had taken out a 49-year lease on a tier of liquid bulk terminals at the port of Vostochny.[48]

Despite its avowed commitment to energy cooperation with China, the Kremlin has apparently found opting for a Nakhodka rather than a Daqing terminus to the Angarsk pipeline irresistible for a variety of reasons. Japan's offer to back the construction expense of a very costly Angarsk pipeline extending all the way to the Sea of Japan with

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Rahman, Bayan, and Jack, Andrew, "Japan lures Russia with $7bn offer on pipeline," *Financial Times*, October 14, 2003.Wonacott *et. al.*, *op. cit.*.

[46] Brooke, "Japan and China battle for Russia's oil and gas," *op. cit.*.

[47] Blagov, "Russia hails partnership with Beijing … sort of," *op. cit.*; McGregor *et. al.*, *op. cit.*.

[48] Shao Da, "Daqing pipeline still most feasible," *china.org.cn*, March 11, 2004 http://www.china.org.cn/english/2004/Mar/89979.htm.

a $5 billion low-interest loan was a necessary if not sufficient part of the equation to secure the favor of Russia's Energy Ministry. More crucial was Japan's eventual willingness to underwrite crude oil field discovery and development efforts in eastern Siberia with an additional $2 billion of discounted financing. This gesture was indispensable because the Kremlin, on the basis of reputable geological surveys, fundamentally believed that without new petroleum exploration and recovery efforts in the Lake Baikal area, not enough proven and readily exploitable crude oil existed in eastern Siberia to warrant a pipeline to Nakhodka rather than a cheaper and hence less risky one to Northeast China. Japan's decision to back off its initial demand that all petroleum piped to Nakhodka be shipped to Japan until the soft loans it extended Russia were serviced was an equally critical factor.

A less recognized but surely significant dynamic that compelled the Kremlin to all but officially announce its binding support for the Angarsk-Nakhodka pipeline was the steadily increasing world market price of petroleum, with no end in sight, as the gamesmanship between Russia, China, and Japan unfolded throughout 2003 into early 2004. With the price of crude oil progressively mounting relative to the cost of building a 3900-km pipeline across challenging terrain, the Kremlin's fears that the east Siberian crude oil fields do not and will not yield enough recoverable petroleum to operate at full capacity a pipeline all the way to the Sea of Japan became less paramount. What is more, with the balance of power in the open global petroleum market playing increasingly more in the hands of OPEC and other major producers, being able to sell east Siberian crude oil to a range of purchasers at spot prices rather than a single purchaser at a negotiated price became all the more appealing to the Energy Ministry and other relevant players in Russia. Ironically enough, by disproportionately contributing to the tightening squeeze on the planet's proven petroleum reserves and the bidding up of world market prices for crude oil, China helped to create some of the circumstances which made routing the Angarsk pipeline to Nakhodka rather than Daqing financially viable. And just as paradoxically, by bidding up world market prices for crude oil and thus facilitating the Japanese underwriting of petroleum field discovery and development efforts in eastern Siberia, China may ensure that one day so much crude oil will flow through a Nakhodka-bound pipeline that extending a branch line to Daqing or some other depot in Northeast China becomes too attractive a prospect for Russia to pass up.

Russia's momentous retreat from approving the Angarsk-Daqing pipeline was not driven by a combination of Japanese haggling and shifting conditions in the international political economy of petroleum export alone. Another source of this retreat was the Kremlin's growing determination to alter the course of Russia's approach to economic development. Russia's alleged boom of the last few years has been thinly predicated upon rising world market prices for its raw material exports (particularly its hydrocarbon exports), but no meaningful revival of its productive capital stock, much less its social infrastructure, has taken place during this time.[49] Throughout 2003 state officials and policy intellectuals associated with Putin's circle made increasingly bold pronouncements about the necessity of taxing windfall natural resource export rents so that these rents would be reinvested in Russia's industrial renewal rather than parked in the ballooning

[49] Cohen, Stephen, "The struggle for Russia," *The Nation*, November 24, 2003.

Swiss bank accounts (or other offshore wealth havens) of the oligarchs.[50] Sensing that the salad days of robber baron *rentier* capitalism were coming to an end, some of Russia's oligarchs began transferring their inflated shareholdings in raw material conglomerates to foreign investors.[51] Forced to defend its new accumulation model before it ever got off the ground, for both symbolic and substantive purposes the Kremlin chose Yukos' principal shareholder, Mikhail Khodorkovsky, as its first target, arresting him in October 2003 on charges of tax evasion, embezzlement, and fraud.[52] With the institutional stability of Yukos, the putative supplier of crude oil in the Angarsk-Daqing pipeline project, thus thrown into doubt, so too was the prospective future of a petroleum pipeline directly linking eastern Siberia and Northeast China. The uncertainty surrounding Yukos and a crude oil pipeline terminating in Daqing bought Japan the time it needed to raise the stakes with its offers to help fund east Siberian petroleum field discovery and development and to allow the offtake from an Angarsk-Nakhodka pipeline to be exported to any and all Asian-Pacific clients.

Even though all signs say go with respect to the Angarsk-Sea of Japan petroleum pipeline, until the Kremlin issues a formal announcement, rather than coyly tipping its hand to the media, there remains a faint chance that Russia's position will shift back in favor of the Angarsk-Daqing pipeline once again. The possibility still lingers that even with Japan's $2 billion commitment to probing and improving the crude oil fields of eastern Siberia, the Kremlin remains skeptical that untapped reservoirs in the vicinity of

[50] Cohen, *op. cit.*; Helmer, John, "Russia split over natural resource exports," *Asia Times Online*, September 20, 2003.
[51] Cohen, *op. cit.*.
[52] Cohen, *op. cit.*.

Lake Baikal contain enough profitably recoverable petroleum to make the Angarsk-Nakhodka pipeline financially preferable to the Angarsk-Daqing pipeline.[53] Until it is absolutely convinced that enough profitably recoverable crude lies beneath the surface in eastern Siberia, it makes little sense for Russia to risk damaging its "strategic partnership" with China by publicly declaring its unwavering support for the Angarsk-Daqing pipeline, especially since Sino-Russian comity is a key ingredient of both countries' recipe for a multipolar world order to counterbalance unilateral U.S. hegemonism run rampant.

Conclusion: regional and global geopolitical implications

Moscow's apparent choosing of the Nakhodka rather than the Daqing pipeline may objectively cause consternation in Beijing, at least for the time being. However, this apparent decision on the part of the Kremlin has a lot if not everything to do with a purely domestic imperative – the need to rein in the petroleum export oligarchs, in the service of a desirable shift in Russian economic development policy. While the CNPC specifically and China generally may be cast in the role of innocent victim in this particular drama, its Russian domestic roots indicate that an overarching retreat from a long-term commitment to Sino-Russian energy cooperation has not taken place. One piece of evidence that attests to this is Putin's recent endorsement of plans to greatly expand Russian shipments of crude oil to China by rail, as a sort of consolation prize for denying China the trunk of the pipeline departing from Angarsk.[54]

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[53] Brooke, "Japan and China battle for Russia's oil and gas," *op. cit.*.
[54] Blagov, "Putin to expand strategic partnership with China," *op. cit.*.

To the minimal extent that the Kremlin's apparent choosing of the Nakhodka rather than the Daqing pipeline signifies any kind of setback at all for Sino-Russian energy cooperation, its impact on the wider, and much more important, pattern of evolving Sino-Russian "strategic partnership" should be trivial. Indeed, I contend that a bundle of synergetically interactive causes-and-effects could, and in my estimation could very well, enhance the Sino-Russian "strategic partnership." This bundle of prospective causes-and-effects is best understood in relation to two powerful trends already in motion: 1) the ongoing plunge of the dollar *vis a vis* the euro in global foreign exchange markets, and 2) the decreasing ability of the U.S. to ensure the stable flow of cheap Persian Gulf crude oil to the world market, given the colossal and not readily correctible failure of its neo-imperialist occupation of Iraq.

The fall of the dollar relative to the euro is cutting more and more deeply into Russia's terms of international trade, because the lion's share of its dollar-denominated petroleum exports are effectively exchanged for European manufactured goods.[55] The continued plummeting of the dollar *vis a vis* the euro may thus force the Kremlin to exercise an option about which Putin has publicly mused: accepting euros rather than dollars as the preferred means of payment for Russia's sale of crude oil on the world market.[56] If for reasons I discussed earlier (including the political chaos that the U.S. has instigated in the Middle East), it comes to pass that China relies less than currently forecast on the Persian Gulf, and more than currently forecast on Russia, as a supplier to

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55 Rifkin, Jeremy, "The perfect storm that's about to hit," *The Guardian*, March 24, 2004.
56 Belton, Catherine, "Putin: Why not price oil in euros?" *MoscowTimes.com*, October 10, 2003; Hoyos, Carola, Christopher Swann, and Andrew Jack, "Putin's idea to price oil in euros may hurt dollar," *Financial Times*, October 10, 2003.

meet its soaring petroleum consumption needs, then China will need a large stash of its euros at its disposal to source that Russian crude oil. Hence China's central bank will be prompted to reposition a sizable portion of its currency reserves from dollars to euros, a crippling blow to U.S. financial-monetary primacy and a striking triumph for the multipolar world order that is the stated aim of the Sino-Russian "strategic partnership." Indeed, a future world order that does not pivot around China exporting labor-intensive consumer goods to the world market and investing the proceeds in U.S. government bonds – or, to put it less kindly, around the super-exploitation of China's export sector working class on behalf of predatory U.S. hegemony – is already assuming embryonic form in China itself and at the Sino-Russian border, what with the CCP recently unveiling its strategy to redirect China's accumulation regime toward the satisfaction of internal social and environmental needs and rising levels of Sino-Russia commodity exchanges and investment deals.[57]

[57] "Development strategy readjustment looming in China," *Xinhuanet*, March 4, 2004; Brooke, James, "Russia catches China fever," *New York Times*, March 30, 2004.