

India, China and the Asian axis of oil

New Sino-Indian partnership in oil and gas could serve as the foundation for an Asian Energy Union.

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In less than a year, India and China have managed to confound analysts around the world by turning their much-vaunted rivalry for the acquisition of oil and gas assets in third countries into a nascent partnership that could alter the basic dynamics of the global energy market.

At stake is not just the issue of joint acquisition, although the most important of the agreements signed in Beijing on January 12 during the visit of Petroleum and Natural Gas Minister Mani Shankar Aiyar envisages ONGC Videsh Ltd (OVL) and the China National Petroleum Corp. (CNPC) [placing joint bids](#) for promising projects elsewhere. Rather, the prospects for Sino-Indian cooperation across the length of the hydrocarbon chain could pave the way for the creation of an Asian energy market and architecture — an Asian axis of oil — with major geopolitical consequences for the United States.

The international market for hydrocarbons is not a free market and has never been one. There is a suppliers' cartel — the [Organisation of Petroleum Exporting Countries](#) — and a well-organised market driven primarily by demand in the advanced industrial economies of the world, all members of the [OECD](#). Trade is conducted in dollars, which effectively ensures that countries around the world hold their foreign reserves primarily as greenbacks. And prices are set on the basis of Western benchmark crudes like West Texas Intermediate and Brent, neither of which represent anything but [a small fraction of the oil that is extracted](#) and traded internationally. So strong is the monopsonist power of the U.S. and Europe that oil exported to Asia from the Persian Gulf [costs as much as \\$2 a barrel more](#). This is the so-called Asian oil premium.

Into this dismal equation must be added two further constants. First, the role of [speculators who trade in oil futures](#) on the New York Mercantile Exchange and International Petroleum Exchange and who have propelled oil prices to absurdly high levels. This problem is only going to get worse. "There's a tremendous amount of speculative money going into energy futures," James Cordier, president of Liberty Trading Group in Tampa, Florida, [told the Associated Press](#) earlier this month. Second, the huge and growing U.S. military presence in Asia that underpins the petro-dollar-unipolar system and is a major source of instability and violence. The position of Asia couldn't be more abject. A continent which hosts the world's largest producers and fastest growing consumers of energy is forced to play second fiddle, relying on institutions, trading frameworks and armed forces from outside the region in order to trade with itself. Such a situation makes for unstable politics and bad economics, not to speak of atrocious geography. Central Asia is close to China and Iran but the U.S. has

spent the better part of a decade trying to make sure pipelines carrying oil and gas from there only go westward. Gas pipelines connecting Iran to India make financial sense but the threat of U.S. sanctions means this project might not get off the ground. If the 21st century is to be an 'Asian century', Asia's passivity in the energy sector has to end.

Objective circumstances favour change. Central Asia has emerged as a major producer and India and China are two of the fastest growing economies in the world. Traditional suppliers, too, have much to gain from an Asian market, especially if this means greater stability and predictability in prices. Saudi Arabia may like high prices but not prices which are "unreasonably high". It is not a coincidence that the first overseas tour of King Abdullah is to China, India, Pakistan and Malaysia and that his agenda, at least in Beijing and Delhi, involves important energy-related initiatives like the [proposed oil reserve facility in Hainan island](#).

For the new India-China energy partnership to work, however, both countries must be prepared to invest the political capital necessary. There are traditional suspicions to contend with, besides the fact that commercial cooperation between companies, even if publicly owned, can run into practical difficulties on the ground. Individual deals will still be contested and should not be the cause of unnecessary heartburn, the recent reports of [Myanmar offering gas to China](#) being a case in point. There is also the negative role of the U.S., which sees India as the weakest link in the emerging Asian chain. Today, Washington is trying actively to divert New Delhi away from the task of creating new regional architecture by dangling the nuclear carrot and the promise of world power status in alliance with itself. India will have to resist these allurements if the Asian project is to go anywhere.

At the core of the new Sino-Indian energy partnership is the proposal for OVL and CNPC to place joint bids for facilities in third countries. Last December, the two companies successfully bought the [al-Furat oilfields in Syria](#) and are today reportedly working on an acquisition in Russia's [Udmurtia Republic](#). There were bitter fights in the past - in Kazakhstan, for example, OVL lost out to the Chinese - and there are some areas where China will outshine India simply because of its deeper pockets and greater strategic élan. A case in point is the China National Overseas Oil Corp decision earlier in January to [purchase the Akpo field in Nigeria](#) weeks after the Manmohan Singh government [vetoed](#) OVL's proposed acquisition of the lucrative field as too "risky". However, the scope for synergy between the two countries is tremendous.

Though some Western analysts are dismissive of Chinese and Indian efforts to acquire "equity oil" - why buy the field when you can always buy the oil on the spot market, they ask - it is this element of the partnership which is likely to prove most irksome to established oil majors in the first instance. Both Chinese and Indian oilmen see the advice against equity oil as self-serving, given that similar counsel could easily be given to the Western oil majors making the same energy acquisitions around the world. As Mr Aiyar told Ma Kai, chairman of China's powerful National Development and Reforms Commission, shortly before the two men signed their MoU, "When companies from the two sides submit a joint bid, no project would be beyond our reach". Senior Chinese oil executives enthusiastically reciprocated these sentiments. "We should go forward together and bid", Chen Geng, president of CNPC, told Mr Aiyar. "Otherwise it is the third party which wins".

Apart from acquiring equity oil and gas, there are other areas where companies from the two countries are planning to cooperate. The Chinese have pioneered oil recovery

technology which helps maintain production at ageing oilfields like Dagang and Daqing at levels far higher than Indian fields of comparable vintage. The Chinese side also excels in basin evaluation and drilling rigs. Indian companies have an advantage in IT-enabled exploration and production services. There is scope to work together but this would mean the Indian security establishment being less paranoid about the involvement of Chinese expertise in domestic, particularly offshore, energy locations. The two countries also need to join hands to develop new energy transport mechanisms, including pipelines within the region and the use of backhaul cargoes in very large crude carriers (VLCCs) and swaps to jointly source crudes from distant sources like West Africa and Venezuela.

Asian oil market in Euros?

Above all, India and China need to keep in mind the big picture – the evolution of an Asian market for crude and products with long-term supply contracts and stable prices, and, eventually, an Asian Energy Union. As Mr Aiyar pointed out in a lecture to Chinese energy specialists in Beijing, the European Union started life as a coal and steel union before growing eventually into a full-fledged economic and political community. Could energy play the same role in Asia with India and China serving as sheet anchors in the way France and Germany did in Europe? With India and China committed to building strategic petroleum reserves, South Korea offering to work on an [‘Inter-Asia Oil and Gas Transportation System’](#), and Iran planning its own [hydrocarbon bourse](#), such an idea is no longer far-fetched.

Linked to an Asian oil market is the billion euro question of non-dollar denominated energy trade. Asian countries collectively hold more than two trillion dollars worth of foreign reserves, the overwhelming share of which is in dollar-denominated instruments. Prudential norms suggest the diversification of the Asian reserve portfolio is overdue. In China, the [State Administration of Foreign Exchange \(SAFE\)](#) has signalled its intention to explore the more “efficient use” of the country’s forex reserves and in India, commentators like [S. Venkitramanan](#) have suggested the RBI start thinking along similar lines.

One way to sustain this shift would be to consider yen or euro-based trading in energy. The economic dynamism of Asia for the foreseeable future suggests what is needed is a strategic rather than tactical change in the composition of reserves. The huge and unsustainable deficits being run by the U.S. are undermining the “oil standard” that has been central to the hegemony of both the dollar and Washington for more than three decades. Relying on the dollar for energy trade will hurt Asia’s producers and consumers alike in the long run. An Asian oil market trading in European euros. Now surely that’s a good recipe for a multipolar world.

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