

A comparison of US and Chinese incentives in winning oil contracts in African countries

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This article compares US and Chinese incentives in winning oil contracts in African countries. Exploration and development of African oil resources has soared, and many nations are competing for these new oil contracts. China has won a significant portion of these oil contracts due to their unique incentive offerings. This report will address a brief history and the development of Sino–African policies and interests, modern US–African energy policy and interests, petroleum opportunities in Africa, China’s growing oil demand, and information on both American and Chinese incentive strategies. This information will be used to compare US and Chinese incentive strategies on winning African oil contracts. Implications for the future will be assessed along with recommendations for making US incentives more competitive in Africa.

If you give a man a fish, you feed him for a day. If you teach a man to fish, you feed him for a lifetime – Lao Tzu

1. Background

The development of China’s African policies and interests

The Chinese have been politically connected to Africa since the 1950s (post-Korean War). During the early stages of Sino–African relations, China endowed support for national liberation movements and direct aid (for instance, Tanzania). By the 1970s, China had more aid projects in Africa than did USA. When the Chinese socialist modernization program gained momentum under Deng Xiaoping in the 1970s, China’s interest in Africa decreased due to Africa’s shortcomings in establishing an efficient economy, the continent’s entrance to international markets (which countered Chinese policy goals) and the increasingly superfluous position the continent took in geopolitics.¹

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¹ Ian Taylor, *China’s New Role in Africa* (2009) 13.

However, several events have led to China's renewed interest in Africa: support during Tiananmen Square, Africa's economic reform in the 1990s, China's developing economy and China's increasing global power. Following the incident at Tiananmen Square in June 1989, Beijing reexamined its foreign policy regarding developing nations. While this event instigated a momentary crisis for China's relationship with the West, Africa's response was quiet and even in agreement. Tiananmen Square negatively impacted the People's Republic of China's (PRC) relationship with the West, but their relationship with developing countries changed from political 'benign neglect' to revamped importance.²

Africa also went through economic reforms in the 1990s, and the Chinese government saw Africa as a renewed opportunity for Chinese business. The Chinese based their decision to pursue African business ventures on their perception that African countries were taking steps towards privatization, participation in international trade and bilateral and multilateral agreement reformation; the Chinese viewed this as an African 'open-door policy.' Further, Chinese businesses saw opportunity in Africa due to the types of goods that Chinese manufacturers produce; these products had greater value in Africa where the buyers would be more interested in purchasing inexpensive products. China's leadership depends on the success and sustainment of the country's economic growth, and ability to obtain raw materials; therefore, Africa's abundance of natural resources matches Chinese domestic and international policy aims.³

China has initiated a more rigorous foreign policy plan to counter the US's international political authority, which, it was concerned, would stifle China's rise as a global political power. This rationale, partnered with China's growing economy, has influenced Chinese leaders to pursue a stronger international position by instituting the concept of multipolarity, which is the creation of flexible political alliances that contain hegemony and to build an improved and 'just' international order. The goal of such a strategy is to gain alliances and positioning in international bodies such as the UN Security Council.⁴

Modern US–African energy policies and interests

US's oil interests in Africa have intensified since the terrorist attacks of 11 September 2001. In the view of the US government, as the political and security environment in the Persian Gulf declines, it is becoming more important to find alternative sources of oil, which must be accessible and reliable, in order to fuel the expanding American demand. According to the African Oil Policy Initiative Group (AOPIG), a Washington DC-based lobby group:

Official statistics indicate that 15.3 percent of US oil imports come from Africa and that an estimated \$10 billion in US oil production investments would flow into West African fields by 2003. At 1.5 million barrels per day, the amount of West African oil

² Ibid 13–14.

³ Ibid 14–15.

⁴ Denis M Tull, 'China's Engagement in Africa: Scope, Significance and Consequences' (2006) 44(3) *J Mod Afr Stud* 459–79. *Academic OneFile* Web 7 Mar. 2010. p. 461

flowing to USA approximates or exceeds the volume of the US imports from Saudi Arabia.⁵

The AOPIG explained that this amplified level of exploration and production is a substantial US capital investment; by the year 2020, over 770 millions barrels of oil will be imported from Africa and, in the next decade, between two-thirds and three-fourths of US foreign direct investment in Africa will support the energy sector. The National Intelligence Council (NIC) estimates that African oil imports to USA will rise to 25 per cent of total imports by 2015. This growth has driven USA to re-examine its strategic and security positions in Africa.⁶

Due to poor relations with Middle Eastern countries and political instability in Latin America, increasing and diversifying the US oil supply is considered an important topic for national security and the economy. The US government views West Africa as the fastest, safest and least complicated path to satisfy national energy needs. USA aims to strengthen and promote American principles with their allies by fostering partnerships which influences energy revenue allocation and expenditures to citizens and not to corrupt leaders. The AOPIG believes that African oil is not an end, but a means; African oil will benefit American energy security and provide opportunity for African economic development.⁷

The AOPIG has pinpointed several issues that will require regional collaboration for a successful solution. Their main concerns centre around deficient infrastructure, health-care facilities, land privatization and sanitary water in addition to the AIDS pandemic. They also stress that land ownership rights are an essential step towards market economy development; property titles fuel private investment towards mortgages and leads to financing economic development. Thus, USA can assist Africa's infrastructure development by providing leadership, trade and support.⁸

2. African petroleum opportunities

Infrastructure development, improved technology (especially in deep water), relative political stability and economic development have sparked African oil exploration and production.⁹ Although almost two-thirds of the world's oil supply is located in Middle Eastern countries, access to this oil has been tightly controlled and much of this oil is expected to stay underexploited for the foreseeable future. In contrast, African nations have been quick to develop their oil resources and have allowed multinational firms to enter; this is exhibited by forecasts of African oil production. The US Department of

⁵ African Oil: A Priority for U. S. National Security and African Development, Proceedings of the Institute for Advanced Strategic and Political Studies held on 25 Jan 2002 in Washington DC IASPS Website 10 April 2010. <<http://www.iasps.org/africa/whitepaper.pdf>> accessed 10 April 2010, 3–4 .

⁶ Ibid 4–5.

⁷ Ibid 8–9.

⁸ Ibid 9.

⁹ Michelle Michot Foss, *Africa: A New Frontier in Oil and Gas Exploration* Geotimes (February 2008). Website 19 April 2010. <http://www.geotimes.org/html?id=feature_africa.html> accessed 19 April 2010.

Table 1. Africa's proven oil reserves in 2005

	No. of Barrels (in billions)	Total (in %)
Libya	39.1	34.2
Nigeria	35.9	31.4
Algeria	12.2	10.7
Angola	9.0	7.9
Sudan	6.4	5.6
Egypt	3.7	3.2
Gabon	2.2	1.9
Equatorial Guinea	1.8	1.6
Congo (Brazzaville)	1.8	1.6
Chad	0.9	0.8
Tunisia	0.7	0.6
Other Africa	0.6	0.5
Total	114.3	100.0

Energy forecasts that total African oil production will rise by 91 per cent between 2002 and 2025. A summary of Africa's proven oil reserves is located in Table 1.¹⁰

From an economic point of view, West Africa is more advantageous than the North Sea or Gulf of Mexico due to its relatively inexpensive commercial exploration and production costs. Drilling ventures in this region have been successful, and the oil often has a high API gravity with low sulphur content contributing to better quality hydrocarbons. There are also transportation advantages as it is closer to US and European markets.¹¹

3. China's growing oil demand

Between 1995 and 2005, China's oil consumption doubled to 6.8 million barrels per day. China became a net importer of oil in 1993 and, according to current forecasts, oil is the main fuel capable of satisfying China's growing transportation and industry needs. Since becoming a net oil importer, China's 'resource diplomacy' has escalated extraordinarily. In 2003, China surpassed Japan as the world's second biggest consumer of petroleum products second only to USA. China's demand has been an issue since, in 2004, China's oil consumption grew by 15 per cent while its output rose by only 2 per cent; the 2004 consumption data represented a 16 per cent increase over what it was in 2003. Chinese oil demand is clearly rising exponentially, and the International Energy Agency (IEA) forecasts that Chinese oil imports will equal that of USA by 2030. Additionally, according to the US Energy Information Administration (EIA), China's oil demand is expected to increase by 130 per cent to 12.8 million barrels per day by 2025.¹²

¹⁰ Jędrzej George Frynas and Manuel Paulo, 'A New Scramble for African Oil? Historical, Political, and Business Perspectives' (2007) 106(423) *Afr Affairs* 229–51. *Academic OneFile* Website 7 March 2010, 240, 241.

¹¹ *Ibid* 241–2.

¹² Ian Taylor, 'China's Oil Diplomacy in Africa' (2006) 82(5) *Intl Affairs* 937–59. *Academic OneFile* Website 7 March 2010, 943.

4. Oil contracts and incentive strategies

American contracts and incentives

In 2004, US direct investment to Sub-Saharan African countries amounted to \$13.5 billion, 23.4 per cent more than in 2003; the top five recipients of this money were Equatorial Guinea, Gabon, Angola, Chad and Nigeria—all oil producers. In 2005, oil imports (crude and non-crude) from Sub-Saharan Africa totalled \$40.1 billion, which accounted for 79.8 per cent of all US purchases in the continent. USA currently imports more oil from Africa than the entire Persian Gulf region; African oil imports constitute about 20 per cent of total US imports.¹³

The US government has implemented a number of strategies in Africa in hopes of creating strong ties for future energy deals. They have used diplomatic methods (eg, establishing embassies), fiscal incentives (eg, financial services from the US Export–Import Bank towards business in Nigeria) and military support to stimulate positive relations with the continent. However, while the US government helped US corporations acquire exploratory and production oil concessions, the Chinese government used bilateral agreements in an effort to secure oil supplies.¹⁴

According to Michael Klare and Daniel Volman, authors of *The African ‘Oil Rush’ and US National Security*, ‘all the major Western powers have long used whatever means and influence are available to them to secure access to African oil, including economic incentives, diplomacy and the provision of arms and military equipment.’ As mentioned above, the USA provides arms and military assistance to friendly oil producers in Africa, therefore China’s aggressive efforts to secure oil assets in Africa combined with their deliveries of arms and other aid is not an originality, but a norm.¹⁵

Chinese contracts and incentives

China offers very favourable and unique incentives to African countries. There are currently more than 800 Chinese companies operating in 49 African countries. China is also the continent’s third most important trading partner just behind USA and France, but ahead of UK.¹⁶ Simply stated, China’s strategy aims to obtain foreign energy resources by signing long-term contracts coupled with buying foreign energy industry assets. Their policy aims to avoid over-reliance on the global oil market by physically obtaining major stakes in Africa’s oilfields or by protecting the right to use them. China considers Africa to be a key location because Chinese companies must go to oil destinations absent of American and European companies.¹⁷

Because China’s oil companies are nationalized, they have different objectives in their search for petroleum contracts compared to nations that utilize privatized oil companies. For instance, China may outbid competitors for African contracts, even if their offer is

¹³ Fynas and Paulo (n 10) 231.

¹⁴ *Ibid* 238–9.

¹⁵ Michael Klare and Daniel Volman, ‘The African ‘Oil Rush’ and U.S. National Security’ (2006) 27(4) *Third World Q* 609–28. *Academic Complete Website* 10 April 2010, 622.

¹⁶ Fynas and Paulo (n 10) 231.

¹⁷ Taylor (n 12) 942.

worth more than the value of the contract. This is because China seeks lasting energy security compared to short-range financial goals private companies must meet to satisfy shareholders.¹⁸ Chinese firms also tend to be less risk averse because they are nationalized and must satisfy political interests instead of investors.

China is also different from Western countries in that they do not require developmental restraints and requirements. In many ways, China's newfound economic power has weakened the Western approach that is based on imposing political conditions and financial reform in exchange for economic assistance. Like other developing nations, China has been supportive of Africa; PRC has provided loans, debt relief, scholarships, training and military supplies without political or economic stipulations in return for their oil business. This has been useful at an international level because African governments use their Chinese support and resources to ward off calls for political and economic reform from international groups like the International Monetary Fund (IMF) and Western governments.¹⁹

Unlike traditional oil concessions and agreements, China offers more than pure financial incentives. China's bids are successful because they pair investment with infrastructure loans for projects that are often neglected or hardly feasible; the infrastructure loans are typically issued at no interest or near zero interest rates which are sometimes settled in natural resources or cancelled completely. For example, China won a contract for a former Shell Oil block, which the largest Indian company had sought, by offering \$2 billion in infrastructure aid. A Nigerian official explained that 'the Western world is never prepared to transfer technology—but the Chinese do, and while China's technology may not be as sophisticated as some Western governments', it is better to have Chinese technology than to have none at all.²⁰ China has also provided educational benefits in their agreements. Approximately, 16,000 African professionals were trained in China from 2000 to 2006 and 15,000 were expected to follow in 2007–2009. China's scholarship offerings have been on the rise: China provided 1,500 scholarships to African nationals in 2005 and 2,000 in 2006, and by 2010 there were an expected 4,000 per year.²¹ These illustrate a sample of China's unique incentives.

Another benefit of Chinese aid is that it is less susceptible to corruption. For instance, Chinese assistance is frequently distributed in ways that prevents corrupt leaders from using it for their personal benefit. The Chinese have provided direct infrastructure (eg, railroads and roadways), medical professionals to those who previously did not have access to healthcare, scholarships for African students to study in China's universities, and capital to entice businesses to invest in Africa.²²

China's aid is not completely independent of political interest. Since 1949, PRC and Taiwan have sought to establish opposing status regarding international recognition and

¹⁸ Ibid.

¹⁹ Frynas and Paulo (n 10) 239.

²⁰ Barry Sautman and Yan Hairong, 'Friends and Interests: China's Distinctive Links with Africa' (2007) 50(3) *Afr Stud Rev* 75–114. *Academic Search Complete Website* 7 March 2010, 80.

²¹ Ibid 88.

²² Ibid 87.

government legitimacy.²³ Along with the recognition of China and Taiwan as one country, Chinese aid also stipulates promotion of China's 'market economy' status which helps oppose antidumping accusations made by the World Trade Organization (WTO). Along the same lines, if China chooses to directly confront Western countries on the international stage, African nations would be a strong ally.²⁴

Comparison of contract strategies

Chinese and American methods for pursuing African oil contracts are clearly very different. The strategies, and drivers of their strategies, differ on three main points: (1) in addition to offering financial compensation, the Chinese offer tangible developmental support in the form of education, infrastructure and technology; (2) the Chinese do not have the same political and developmental requirements that the US must abide; and (3) the Chinese have different objectives than the US given the fact that their companies are nationalized and they do not have shareholders.

From a commerce perspective, successful Chinese bids typically exhibit low labour costs, tight profit margins and quick project turnaround. While Western corporations often require a 15–25 per cent rate of return, most Chinese companies will accept less than 10 per cent and many agree to 3–5 per cent. For instance, in Ethiopia, PRC firms made unprofitable bids to establish their business there; the Chinese contractors that built Ethiopia's roads only required a three per cent profit whereas Western firms would need at least 15 per cent. In addition, lower salaries and decreased profit margins are also a result of competition between China's state-owned firms.²⁵

China's lack of political and developmental stipulation-tied aid is a major factor for African concessions and agreements. As Julius Nyerere, the first President of Tanzania, once stated, 'the Chinese people have not asked us to become communists in order to qualify for this loan. . . They have never at any point suggested that we should change any of our policies – internal or external.'²⁶ One Kenyan spokesperson also commented that, 'you never hear the Chinese saying that they will not finish a project because the government has not done enough to tackle corruption. . .if they are going to build a road, then it will be built.'²⁷ Additionally, China does not implement political conditions with its aid, except that recipients must preserve diplomatic relations with PRC, and not Taiwan.²⁸

The Chinese also benefit from their relative lack of history in the African continent. While some view these Sino–African relations as imperialistic, there are several distinct factors that separate Chinese relations with Africa from those of the EU and USA. Looking back into history, these differences are: (1) China was never a participant in the transatlantic slave trade; (2) there has been no Chinese colonialism, genocide and/or

²³ Taylor (n 1) 27.

²⁴ Sautman and Hairong (n 20) 86.

²⁵ *Ibid.* 86.

²⁶ *Ibid.* 87.

²⁷ Tull (n 4) 466–7.

²⁸ Sautman and Hairong (n 20) 87.

occupation in Africa; (3) China accepted the African liberation process with diplomatic, political, material and military support; (4) both China and the African Union (AU) formed the part of the South – South bloc in the WTO which contests the patenting of life forms supported by American biotech corporations; and (5) China has not been associated with the policies that impoverished Africa for the past three decades.²⁹

Thus, by proposing a blend of political and financial incentives to their African allies, the Chinese government is effectively communicating that Sino–African cooperation will be a ‘win–win situation’ for both parties. This is exemplified by China’s efforts to prevail as both a more advantageous partner than Western countries, but also as a better option for the African continent. China has sternly renounced the legitimacy of foreign intervention into domestic affairs, and the PRC’s policies mirror their ‘state-centred orthodoxy’ such that, political issues regarding Taiwan aside, no political assistance are tied to the development support.³⁰

5. Implications for the future

While China’s current African holdings are limited in size, there is significant potential for future Sino–African oil agreements. Currently, China has not ventured into Africa’s oil reserves to the extent that media coverage has implied. Wood Mackenzie, an energy consultancy, estimates Chinese firm hold under 2 per cent of Africa’s known oil reserves. Erica S. Downs of the Brookings Institution goes on to explain that the majority of African oil resources held by Chinese companies are of minimal interest or have already been relinquished by international oil companies (IOCs) due to their size or quality.³¹

Another key concern over Sino–African relations is the relative control the Chinese have over agreements and their potential to exploit African nations. China may not realize the long-term affects of their policies towards Africa; corruption and political instability have long plagued the nation and while some venal leaders benefit from this ‘friendship’, most African citizens likely oppose such a relationship. Africa is also unprepared to deal with the onslaught of Chinese contracts, and as one Kenyan newspaper explains, ‘China has an Africa policy, but Africa doesn’t have a China policy’. This coincides fears that while China preaches shared trust, China may cheat Africa as the West did.³² There is mounting indication of hostility towards Chinese oil companies in Africa as they appear to receive special favours and protection by the state governments. With this in mind, the Chinese government must be prepared for potential negative reactions from bothered and excluded locals as their policies may have unintended and unforeseen consequences.³³

²⁹ Horace Campbell, ‘China in Africa: Challenging US Global Hegemony’ (2008) 29(1) *Third World Q* 89–105. *Academic Search Complete Website* 7 March 2010, 100.

³⁰ Tull (n 4) 466.

³¹ Stephanie Hanson, *China, Africa, and Oil Council on Foreign Relations* (6 June 2008). <<http://www.cfr.org/>> accessed 10 April 2010.

³² Taylor (n 12) 952–3.

³³ *Ibid* 954.

While a Heritage Foundation report suggests that USA, in conjunction with other nations, should counter the Chinese influence by 'linking economic incentives, diplomatic support, and other desirables to progress in economic liberalization, political freedom, enhanced transparency, and accountability', this is unlikely to work due to the fact that African leaders, especially those already working with the Chinese, would trade their 'no questions asked' support for aid that is tied to political conditions as well as the fact that many African leaders do not have true interest in the Western view of 'progress' (ie, liberalization, political freedom, transparency and accountability). One potential suggestion for countering Chinese influence in Africa is to cooperate with China when they adhere to 'governance norms' and on mutual interests.³⁴ For instance, Chinese participation in UN peacekeeping operations in Africa, financial support for the emerging African Union, and environmental damage avoidance are relatively simple areas of potential partnership.³⁵

The US government needs to take a very serious look at its current policies towards both Africa and China. The democracy-oriented US government is fundamentally different from that of the Chinese, and while the Chinese may be able to seek out contracts that US oil companies would not be able to obtain (due to a lack of projected profits), the US can offer contracts beneficial to both USA and Africa. USA is an established leader in technology, quality, safety and education amongst other valuable services to society. To make US bids on African oil blocks as competitive (or more competitive) as the Chinese offers, the American government should support and provide incentives to US oil companies who offer more than monetary compensation for oil contracts. US oil companies have access to and the capabilities to provide infrastructure, education/training and technological transfer just as the Chinese do. Policy and legislation that supports US companies in pursuing these efforts, if done correctly, will not only promote the US position in Africa, but has the potential to boost corporate returns for those companies. If the American companies negotiate oil concessions and agreements that provide for a combination of financial, infrastructure, training and other non-monetary forms of compensation, the companies will stand a better chance of winning contracts; this will ultimately improve US–African relations while simultaneously boosting the corporations' potential for winning future contacts as the African leaders and communities realize there is a win–win situation.

³⁴ Ibid 958.

³⁵ Ibid 959.