



The Energy Dimension in China's Arctic Interests

Christopher Weidacher Hsiung

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China's increasing demand for oil and gas means that it is searching abroad to secure new sources of imports. With its rich resources, the Arctic region could serve this purpose, and Chinese oil companies have shown interest in exploration and production opportunities there.

Decades of high and sustained economic growth have substantially increased China's need for energy. China is the world's second largest economy and the world's largest energy consumer. Importantly, as domestic production has not kept pace with raising consumption levels, China is forced to import most of its oil and natural gas. China today is the world's second largest oil importer and third largest importer of natural gas. Crucially, China's oil import dependency is high and increasing. For instance, in 2016 more than 60% of China's oil demand came from overseas imports, up 3.5% from 2015.

To meet its growing energy import demand, China has, in the last decade or so, embarked on an energetic effort to search for overseas supplies. A central objective has been to diversify the origin of its oil and natural gas sources, and means of delivery. Today, China imports oil from the Middle East and North Africa, Latin America, Central Asia and Russia, via the sea, railway and oil pipelines. China imports liquefied natural gas (LNG) from a variety of sources (for instance from Qatar, Australia, Indonesia, and Malaysia) but also pipeline natural gas from Central Asia, Myanmar and has contracted large future imports from Russia.

However, more than 50% of Chinese oil imports originate in the Middle East and North Africa and up to 80% of China's maritime oil import must travel through the narrow Malacca Strait, a stretch of water between the Malay

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Peninsula and Sumatra. In the eyes of China's strategic planners, this makes their country vulnerable to potential disturbances of oil supplies, not only due to volatile political conditions in these regions but also, however unlikely, a potential U.S. naval blockade.

Enter the Arctic region. According to the widely cited 2008 report by the [United States Geological Survey \(USGS\)](#), 30% of the world's undiscovered natural gas and 13% of the world's undiscovered oil is estimated to be in the Arctic region. Energy imports from the Arctic, Chinese strategists calculate, would help mitigate China's supply and transport vulnerabilities by presenting an alternative to existing import sources and delivery routes.

Expanded engagement

China is not an Arctic littoral state, but officially defines itself as a “[near-Arctic state](#)”. China has in recent years incrementally stepped up its engagement in the Arctic region. China sought, and in 2013 secured, permanent observer status in the Arctic Council (AC), granting Beijing a new platform, albeit with limitations, to participate on issues regarding Arctic governance. Importantly, China acknowledges and respects the sovereignty claims and rights of Arctic states, a pre-condition for observer membership status acceptance in the Arctic Council. China also recognizes the United Nations Convention on the Law of the Sea (UNCLOS) as the legal foundation governing the Arctic. This helped alleviate concerns over China's growing Arctic presence, which some viewed as potentially [challenging the regional Arctic order](#).

China is active in scientific research in the Arctic pertaining to global climate change. While such research is sometimes brushed off as a mean to hide China's other goals, the daunting environmental challenges currently facing

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China surely motivates genuine international scientific climate work and collaboration in the Arctic. China's icebreaker, The Snow Dragon (*Xuelong*), has conducted seven scientific research expeditions as of 2016 and a second icebreaker under construction (ready to sail by 2019). In 2004 the Yellow River Station (*Huanghe zhan*) research facility in Norway's Svalbard was established. China is also engaged in numerous scientific bilateral and multilateral cooperation projects with Arctic States, for instance the China-Nordic Arctic Research Center, while simultaneously boosting its domestic polar competence.

The EU is China's biggest trading partner and China is the EU's second biggest. As the Arctic ice-cap continues to retreat, opportunities for new trade links between transiting the Northern Sea Route (NSR) from China to Europe are opening up, shortening the shipping time and fuel savings considerably compared to the conventional route through the Malacca Strait and Suez Canal. There have been some optimistic estimates made by the Chinese. For instance, according to one figure, 5 to 15 of China's total trade could use the route by 2020, if constructively prepared. China's largest shipping company, China Ocean Shipping Company (COSCO), has over the years conducted a few, but increasing, intra- and trans-Arctic voyages and announced that it plans to begin with regular trans-Arctic sailings. However, prospects such as the above estimate seem overly optimistic as utilization of the NSR is dependent on variety of factors (commercial, infrastructure, technical, environmental etc.), reflecting overall low numbers of trans-arctic maritime trade. Importantly, most of the Chinese commercial actors remain hesitant to make large-scale investments and the optimistic scenarios must be taken with caution.

Energy – a cautious tale

Natural resources, particularly oil and gas, constitute another area of Chinese interests in the Arctic, according to some the principle motive. While the Chinese government has of late been more open about its **economic interests** in the Arctic, and also taken steps to promote energy bilateral cooperation with Arctic states, **notably with Russia**, Chinese commercial players on the ground have been cautious. It is often stated by the industry itself that China lacks the technical skill to operate in harsh Arctic conditions. The goal for Chinese oil companies is instead primarily to learn and obtain technical know-how from more advanced international companies. Western sanctions against Russia, due to the annexation of Crimea in 2014, further complicate the situation. While Russia has turned increasingly to China for capital and investments, the lack of technological skill limits China's actual participation in exploration and production. Moreover, the current low oil price has made the global energy market a "buyer's market". Today's big buyers such China have more options. In other words, Arctic oil and gas needs to be "cheap" enough to be commercially attractive compared to other available import sources.

This has undoubtedly impacted on the scope and nature of **concrete Chinese Arctic energy projects**. Most of what has been done is limited. For instance, the attempt to explore oil and gas in the Dreki area off the coast of Iceland by China National Offshore Oil Corporation (CNOOC) together with Icelandic Eykon Energy and Norwegian Petoro remains uncertain. The often noted purchase by CNOOC of Canadian Nexen in 2013 for 15.1 USD billion and the company's investments in Canadian oil sand have yielded limited returns so far. Russia's Rosneft has invited China National Petroleum Corporation (CNPC) to explore three offshore fields in the Barents and Pechora Seas, but open information on progress is scant.

There is one project, however, which seems to have materialized significantly, namely CNPC's involvement in the **Yamal LNG terminal** project in Russia's Arctic Siberia. The project is one of the Arctic's most ambitious infrastructure projects with an estimated cost of 27 USD billion. The terminal will supply customers with LNG gas and aims at being operational by 2017, offering a future annual capacity of around 16.5 million metric tons per year. CNPC entered the project in 2013 in buying a 20% equity stake while committing to import 3 million tons LNG annually for a 20-year period (price so far undisclosed). Then in 2015 China's Silk Road Fund bought 9,9% making China the project's second largest investor after Russia's Novatek with owns 50,1% percent and French Total with remaining 20%. The Export-Import Bank of China and China Development Bank, China's "political banks", in 2016 offered loans of a total of 12 USD billion, lending important financial support to the project. Additionally, Chinese companies supply Arctic modules for the construction of the terminal. Finally, Chinese shipping and construction companies are involved in the manufacturing of specialized ice-breaking LNG carriers which will be used for shipping LNG to customers. As of 2015, Chinese shipping companies have been involved in the construction of fourteen of the fifteen commissioned.

Conclusion

China's Arctic energy interests have been limited. The Yamal LNG project is the only significant Chinese project, in part reflecting changing external circumstances as Russia's isolation due to western sanctions literally opened up for more Chinese capital, and thus involvement. Despite the current modest Chinese concrete involvement, Arctic energy will nevertheless play a part in China's overall energy strategic outlook in the years to come as demand for oil

and especially natural gas will continue to be substantial. Arctic energy imports will not replace any of China's main energy import sources, but more likely serve as an (limited) additional supply source.

Image credit: [Timo Palo/Wikimedia](#).

Christopher Weidacher Hsiung is a researcher at the Asia Centre at the Norwegian Institute for Defence Studies (IFS) and PhD Candidate at the Department for Political Science at Oslo University. His main research areas include China's foreign and security policy, Sino-Russian relations and China's Arctic interests.

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