Geopolitics, Global Patterns of Oil Trade, and China's Oil Security Quest

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Summary

Safety and certainty in oil, according to Winston Churchill, lie in variety. Unlike many policymakers, some economists maintain that the world oil market is "one great pool," because crude oil is fungible. If the oil market is a single integrated world market, special arrangements from importers to "secure supply" and exporters' attempts to find a "secure outlet" for their crude oil make no economic sense. For instance, the round trip voyage from Venezuela to China is almost five times longer than that to the US Gulf ports, and hence any effort to diversify Venezuelan oil sales away from the United States to China appears to be cost ineffective.

This paper examines the effect of international relations on global oil trade pattern. Using voting records for the United Nations General Assembly to measure the state of international relations, we estimate a modified gravity model in a panel data framework over the period 1962-2000. Controlling for oil exporters' endowment, potential supply disruption due to civil conflict, other standard gravity controls, as well as exporter and year fixed effects, we first show that private energy companies based in the United States import significantly less crude oil from US political opponents. The result is robust to controlling for economic sanctions and militarized interstate disputes, suggesting that the political oil import diversification is more than a wartime phenomenon. A similar oil import pattern is observed in China, where only a few national oil companies control the oil sector. While the incentives to diversify are stronger for both the United States and China when the exporters are nondemocratic, import sanctions have opposite effects on oil imports into the United States and China. Finally, we document that there is no such oil import pattern in other non-major power oil importing countries.

To the extent that oil companies in major powers do not minimize their transportation cost of oil imports, we have identified an economic cost of oil dependence even in the absence of foreign intervention or interstate war. Quantifying this cost of oil dependence provides a useful step towards a better understanding of the relationship between energy policy and foreign policy. When major powers import more oil from their political allies, China's quest for oil raises tensions with the United States for two reasons. On the one hand, if China is allied with the political opponents of the United States, a political tension is created because according to the United States some of these states are sponsors of terrorism. Our analysis suggests that Chinese companies defy sanctions imposed by the United Nations, because import sanctions have opposite effects on oil imports into the United States and China. On the other hand, if China is allied with the political allies of the United States, an economic tension is created because both major powers are competing for the same pool of crude oil. If oil trade and political distance simultaneously affect each other, in the long run, the economic tension may translate into a political one.