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* 'Asia Pacific region' as used here includes East Asia, Southeast Asia, South Asia, Oceania, and the Russian Far East.

Protectionist Capitalists vs. Capitalist Communists: CNOOC's Failed Unocal Bid In Perspective

by Francis Schortgen

ABSTRACT

China, Inc. is on the move. Whether or not this presents a welcome development for particular political and/or business interests – not just in the United States but worldwide – it is a reality that cannot be ignored, wished away, or warded off with protectionist measures in the medium- to long-term. The real question is: What is an appropriate China strategy in the age of Chinese multinational corporations? How and to what extent does the U.S. government's current China strategy have to be revised so as to fit the new reality?

The protectionist impulse that the U.S. displayed in the CNOOC-Unocal debate is a clear manifestation of the inherently flawed nature of the United States' current China policy, at least in the economic realm. Contrary to widespread perception, U.S.-China economic relations in general, and Chinese merger/acquisition attempts in particular, do not connote a zero-sum game. However, politically motivated actions, such as the one displayed in response to the proposed CNOOC deal in 2005, will provide fertile grounds for outcomes that most decidedly will not be in the best interests, whether economic, national security or otherwise, of the United States.

On 23 June 2005, China National Offshore Oil Corporation, Limited (CNOOC) announced an unsolicited takeover bid for El Segundo, California-based Unocal Corporation. The proposed merger came on the heels of a string of notable recent overseas acquisitions by Chinese companies. These have included Lenovo Group's $1.75 billion purchase of IBM's PC division in December 2004 (completed on 1 May 2005); Haier Group's failed bid, launched in June 2005, for Maytag Corporation; and TCL International Holdings' acquisition of both TV and DVD businesses of France's Thomson SA, announced in November 2003. These are but some of the more prominent endeavors of China's "Go-Out" strategy in recent years.

The rising trend of outward investment by Chinese multinational companies (MNCs) is an unmistakable testament to Chinese economic prowess and the international ambitions of its major corporate groups.[1] The stated goal is an aspiration to see 50 mainland companies break into the ranks of Fortune 500 companies by 2010. Though flush with "Chinese dollars," it remains to be seen how aggressively and/or how soon leading mainland Chinese companies will venture to acquire U.S. corporate entities in the wake of the strong opposition to CNOOC's failed bid. I argue in this paper that the United States' current China policy is inherently flawed. Washington is badly in need of a fundamental and coherent review of its strategic assessment of China. Contrary to stated arguments that U.S. policies toward China have been, and continue to be, dominated largely by narrow commercial concerns, I maintain that the CNOOC case is one of the most concrete examples yet of unfounded and exaggerated fears driving policy decision-making towards China. The policy dilemma that underlies much of the heated reaction to the CNOOC bid is the perennial question of how to deal with a rising and ever more economically powerful China.

China, Inc. on the Move: From Strategic Partner to Strategic Competitor

American views of China have a documented history of oscillation between fear, affection, and strategic rivalry.[2] In 2001, the incoming George W. Bush administration was quick to distance itself from the Clinton administration's recognition, however tepid and brief it was, of China as a strategic partner. Rather, China came to be viewed increasingly through the lens of strategic competition. Though the "strategic competitor" label was dropped virtually overnight after September 11, 2001 when preoccupation with China, at least from the 'threat' perspective, was relegated to minor secondary status by the Al Qaeda attack and the ensuing focus on waging a "War on Terrorism."

Nevertheless, the notion of competition and challenge has never fully dissipated. Indeed, over the course of the 1990s and into the 21st century, a persistent ebb and flow of fixation on the China challenge took center stage. Defined both in military terms and in economic and trade considerations, China was rarely out of the spotlight.

Indeed, China's growing economic influence and emerging worldview – one in which China is showing subtle signs of shedding the image of a reactive and passive international actor – have led to an exponential proliferation of alarmist predictions from the 'China Threat' or 'China Challenge' schools of thought. China's military modernization and national security strategy,[3] emerging military threat perceptions,[4] the volatile Taiwan Straits issue,[5] and China's rapidly expanding economic and trade challenge and its impact on the global business system[6] are generally the themes receiving some of the broadest and most in-depth coverage.

Amid all these relevant issues, however, China's single most dramatic and far-reaching challenge largely takes on an air of secondary importance, despite the ubiquitous presence of factors that are fueling it. And that is the rising challenge in global energy markets; a challenge that, comparatively speaking, at least was more or less marginalized until the recent highly publicized attempted Chinese forays into the U.S. oil market. How China will meet rising energy demands and address the issue of energy security will determine "whether oil becomes a source of tension or a spur to China's deeper integration into the global economy."[7] China's economic rise is impacting geopolitics in fundamental ways and, although in a more indirect manner, rewriting economic rules.

If viewed in a broader context, the politically-charged reaction triggered by the CNOOC bid for Unocal conjures up memories of a 1980s movie, starring Japan, Inc. Whereas the first version featured what many perceived to be a 'new model of capitalism,' created by Japanese banking and governmental policies, the China, Inc. sequel galvanizes popular feelings more easily and makes headlines more prominently, due in no small part to the fact that the challenge is emanating from a socialist/communist base.[8]

The lessons of the 1980s Japanese challenge seem to have largely been forgotten in the United States – if not in corporate boardrooms, then certainly in the maze of what is political Washington. How long before predictions of "China as Number One" will grab headlines? The emergence of China-inspired versions of Clyde Prestowitz' Trading Places[9] and Lester Thurow's Head to Head[10] (recognized for their penetrating analysis of the looming Japan challenge and its consequences at the time) is not a question of if but merely of when. Oded Shenkar sees in the magnitude of China's economic challenge a potential to trigger a significant backlash in the U.S., driven by "geopolitics, animosity perceptions, and other 'nonrational' considerations."[11] He further argues that commonly accepted views on the nature of national and firm competitiveness, the value of geographic proximity, and the cost of market entry and exit will be questioned by the sheer extent of the Chinese business challenge.

Considering the pronounced aggressiveness with which Chinese multi-national corporations (or MNCs) are expanding overseas and making great strides towards heightened global competitiveness, it is rather disconcerting, if not alarming, that this phenomenon has thus far failed to garner the scholarly attention it deserves. A recent study by Ernest Preeg, a noted international economic and foreign policy specialist and senior fellow in trade and productivity for Manufacturers Alliance/MAPI, constitutes the highest-pitched wake-up call thus far. China, he concludes, "is on track to become an advanced technology super state and the principal U.S. rival in the sector."[12]

Many recent forays by Chinese MNCs into overseas markets have been scrutinized through the political lens of industrial and economic competition. Whereas the Chinese challenge is primarily depicted as potentially undermining national security (to varying degrees), it has not prompted an equally necessary appraisal of U.S. industrial and corporate competitiveness. Unfortunately, the rather narrow-minded framing of the China challenge to-date merely exacerbates the propagation of an outdated understanding of the dynamics driving Chinese economic growth and of the motivations and capabilities of many Chinese MNCs.

It would be foolish to seek comfort in the notion that China's economic reform efforts since the early 1980s have only been partially successful. True, many hurdles and challenges prevail in China's quest to improve global competitiveness, lest the forces of globalization help to marginalize the various effects of reform, much as they have done in Russia.[13] In sizing up the China challenge, it is indeed to be hoped, paraphrasing Nolan, that the U.S. will seek truth from facts rather than indulging in misplaced and outdated illusions.

What China Strategy?

Other than highlighting China's growing integration into the world economy and the coming of age of its multinational corporations, the CNOOC move has certainly laid bare a disturbing reality. There is currently an utter lack of a coherent China strategy in the United States, above and beyond touting the need to keep a watchful eye on the country's military modernization and to plan for appropriate contingencies. Not only did the unsolicited bid blindside commercial and national security officials, it prompted a rash and irresponsible response that not only further exposed Washington's strategic incoherence concerning international economic and commercial matters but, even more ominously, depicted the United States as backtracking on its free-trade mantra.

Meanwhile, in the characteristic fashion of China hawks and national security advocates, it did not take long before a new wave of alarmist predictions found willing advocates. One the most ludicrous observations was offered by James Woolsey, former director of the Central Intelligence Agency (CIA) and now a vice-president of Booz Allen Hamilton, when he described CNOOC as the corporate vehicle of "a Communist dictatorship."

On the other hand, Clyde V. Prestowitz offered one of the most astute and even-handed interpretations. In line with his argument of the shift of wealth and power to Asia,[14] he succinctly captures the hypocrisy of the prevailing U.S. attitude towards trade and economic relations. "We handed China the money they are using to try to buy Unocal," he says. "And now we're telling the Chinese, please keep investing in our bonds but you can't invest what amounts to a sliver of their surplus in an oil company."[15]

Economic and commercial policies are the result of actions taken by the Department of Commerce, in cooperation with other relevant departments, depending on the nature of the issue(s) at play. In addition, the U.S.-China Business Council is a strong advocate for strengthening China-U.S. economic and commercial relations. Under the rules governing international investment in the United States, foreign companies contemplating a merger and/or acquisition transaction in the United States may be subject to (1) the Hart-Scott-Rodino Antitrust Improvement Act of 1976 (HSR Act), and/or (2) the amended Section 721 of the Defense Production Act ("Exon-Florio provision").

Implementation of the Exon-Florio provision falls under the purview of the Committee on Foreign Investment in the United States (CFIUS). Established in 1975 by Executive Order 11858, its original function was to monitor and evaluate the impact of foreign investment in the United States. As a result of Executive Order 12661, issued in 1988, the role of CFIUS expanded. Notices of foreign acquisitions of U.S. companies are now to be filed with CFIUS, which is then tasked with determining potential national security ramifications of a particular acquisition that might warrant an investigation. If that is deemed to be the case, CFIUS is then to undertake such an investigation and to submit a recommendation to the president of the United States.

Voicing strongly-worded concerns and expressing overt opposition to CNOOC's attempt to buy Unocal, spanning financing and national security points, Congressional activity against the bid gained momentum rather quickly, as shown with passage of an amendment (H. Amdt. 431) to House of Representatives bill 3058, agreed on June 30, 2005, and Senate Bill 1412 introduced on July 15, 2005.[16] Senators Conrad (D-ND) and Bunning (R-KY) pushed for detailed investigation into financial backing provided by the Chinese government for the proposed deal.[17]

The Age of Chinese Multinational Companies

McKinsey & Co. has noted that recent M&A activities of Chinese companies (see Table 1) may increasingly be driven not only by global aspirations, but are likely an obvious adaptation to rising competition in the domestic market and a calculated move to reduce what appears to be a widening gap in capability vis-à-vis foreign competitors.[18]

Apart from the recent CNOOC bid, the most obvious manifestation of the growing prominence and aggressiveness of China, Inc. was the successful takeover of IBM's personal-computer division by China's Lenovo Group. This merger and acquisition trend will only increase in the future, as Chinese corporations are determined to extend their reach, marketing, and managerial experience.[19] At the risk of implying a direct correlation between the limited research on the topic and the lack of coherent understanding regarding the significance of this development, and the political, corporate and economic policy fine-tuning it compels, the literature on the coming of age of Chinese MNCs is still in its infancy. Some of the more significant work done to date includes studies on motivations and implications of outward investment by Chinese MNCs[20] and a recognition of their changing nature.[21] Gu (2005a) and Beal (2006), meanwhile, offer one of the few attempts at conceptualizing and contextualizing the Chinese MNC phenomenon and how it is likely to affect global business in the near future.[22]

CNOOC – At the Forefront of China's Oil Quest

From a Chinese perspective, the extent of oil diplomacy and the commitment to developing an outward oil economy is as understandable from a national security and energy supply rationale as is the U.S. opposition to the CNOOC move. Underlying China's diversified and omni-directional oil investment is a simple, determined, rational decision-making and risk assessment regarding oil supplies. Continued, uninterrupted energy supply is critical to China achieving future economic growth targets. The sustainability of high economic growth rates is crucial to the maintenance of social stability, political legitimacy of the Chinese Communist Party (CCP) (already weakened by the bankruptcy of Marxism-Leninism) and the commitment to SOE reform. The short-term adverse consequences of breaking the proverbial "iron rice bowl" only reinforce the urgent need for maintaining current levels of economic growth, lest the regime be confronted with growing levels of social unrest.

Table 1: China's Recent M&A Scorecard

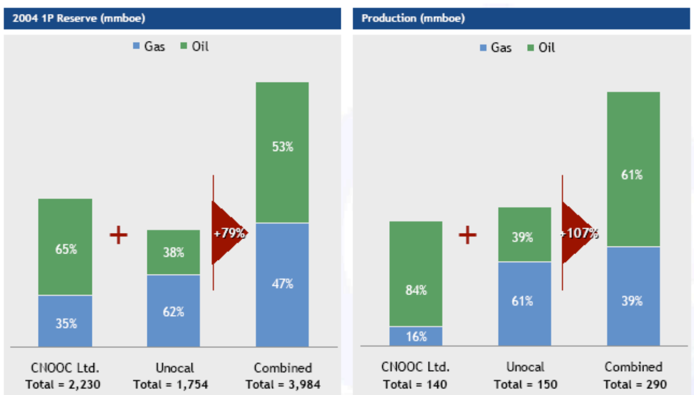
Year/ Month	Chinese Company	Target Company	Outcome
2005/08	China National Offshore Oil Corp. (CNOOC)	Unocal (U.S.)	Bid dropped
2005/07	Nanjing Automobile (Group) Corp.	MG Rover Group (UK)	Successful
2005/07	Haier Group	Maytag (U.S. appliance maker)	Bid dropped
2005/07	CITIC Resources	Thai Petrochemical Industry	Bid dropped
2005/06	Consortium, including China National Petroleum Corp. (CNPC)	Pogo Producing (U.S. energy firms; targeting its Thai oil and gas assets)	Failed
2005/03	China National Metals and Minerals Corp. (China Minmetals)	Noranda (Canadian copper a zinc miner)	Bid dropped
2005/01	Sinochem	Inchon (South Korean oil refiner)	Failed
2004/12	Lenovo	International Business Machines (U.S., PC business)	Successful
2004/07	Shanghai Automotive Industry Corp. (SAIC)	Ssangyong Motor Co. (South Korea)	Successful

Stirring the fires of national pride and nationalism is an opportunistic means to garner support for matters of crucial importance to the state. In the case of China, nationalism has served a rather useful tool in recent years to temporarily divert attention temporarily from matters of pressing concern to the CCP. CNOOC's management labeled the proposed Unocal takeover bid Operation Bao Chuan, or Operation Treasure Ship, in part to capitalize on feelings of national pride conjured up the original Bao Chuan. The historical reference is to Admiral Zheng He's fleet of treasure ships that embarked on ambitious naval expeditions in the 14th century under the Ming Dynasty. The political motive of the extraordinary naval expeditions of the Chinese imperial fleet at the time rested with the Yongle Emperor Zhu Di's desire to increase the list of tributary states to the Middle Kingdom (the literal translation of Zhongguo, the Chinese word for China). The contemporary equivalent to Zheng He's naval expeditions is the tireless search for exploration and development opportunities of a modern-day treasure: black gold. High-level Chinese emissaries are crossing the globe daily in an effort to secure rights in foreign oil fields, sign strategic partnerships with national governments and/or multinational oil companies. The motives of the modern-day Bao Chuan operations are obvious: securing supplies to sustain rising energy demand and consumption levels.

The unsolicited CNOOC bid for Unocal is the highest-profile manifestation of this outward-looking oil economy to-date. Its importance, impact, as well as intended/unintended consequences can be assessed on a multi-faceted levels-of-analysis approach. Geo-political and geo-economic considerations of Chinese oil politics, most appropriate for a systemic-level analysis, are beyond the scope of this paper. Here I shall limit myself to a discussion of the general trade-related issues and concerns that underlie the CNOOC-Unocal merger proposal as well as the corporate strategic considerations that prompted the CNOOC offer.

The lure of Unocal as a lucrative acquisition target influenced CNOOC's corporate motivations in many respects. Indeed, in corporate strategy terms, a successful merger would certainly have filled CNOOC's coffers. CNOOC would have realized a significant increase in oil reserves and boosted its production capacity. In addition, a more stable division between oil and gas assets (see Figure 1) would have contributed positively to a reduction of the company's "exposure to commodity price cyclicality."[23] CNOOC management pointed to growth platform, optimization of investment programs, proven management and world-class technical expertise, and the potential for the creation of an Asia-focused energy company with a leading regional gas business as notable strengths and opportunities in its strategic business analysis of the proposed CNOOC-Unocal merger.

Figure 1: CNOOC-Unocal Combined Asset Portfolio
Source: www.cnoocltd.com/investor/channel/Investor_Presentation.asp



The planned merger would have been compelling in terms of scale, industrial logic, value-creation opportunities, and enhancement of technical skill base. Additionally, in the eyes of CNOOC top management, it offered a nice fit with the company's overall strategic orientations, which primarily centered around three themes: (1) a focus on production and reserve growth; (2) development and expansion of natural gas business; and (3) maintenance of industry-leading cost management and financial discipline.

The CNOOC Bid in Context

Washington's reaction to the surprise takeover bid suggests the relative unease of the champion free-trading nation in an era of globalization that coincides with the inevitable rise of China to economic superpower status. Accounting for the general receptiveness of alarmist scenarios painted by the chairman of the U.S.-China Economic and Security Review Commission (USCESRC), among others, is a calculated and purposeful omission of relevant information concerning the CNOOC bid.[24]

It was a performance that rivals the best of targeted public relations and interest group lobbying efforts. It spread fears and fantasies that have ultimately struck a most receptive chord in Washington policymaking circles, and unfortunately have also contributed to a reinforcement of distorted perceptions and stereotypes, including the alarmist predictions of the "coming conflict with China."[25] The result is not only a misconstrued picture of China that will only result in further complicating the formulation of a sound China policy, but also a negative boomerang effect. Though the U.S. may have succeeded in protecting national security concerns, it came at the cost of being caricatured as "protectionist capitalists," compared with "capitalist communists."[26] It does not take too much imagination to figure out which one of these labels is the least flattering.

In hindsight, the timing of the CNOOC bid could not possibly have been worse. Most notably, some of the key issues currently troubling U.S.-China relations should have given top management a pause: the growing 'China bashing' momentum, (stoked by concerns over an ever-rising U.S. trade deficit with China), charges of job dislocation due to offshoring in various industrial sectors,[27] pressures for revaluation of the Renminbi (RMB, or yuan), continued prevalence of intellectual property right violations that see U.S. corporations foregoing significant portions of revenue flows in China, and charges that Beijing is unwilling to use the full extent of economic leverage over North Korea to work towards a diffusion of the festering nuclear crisis.[28] It does not take the benefit of hindsight to realize that a bid by a Chinese company under these circumstances was destined to run into a wall of opposition. In this context, it is hard to take seriously the allegations of vocal opponents who charged that the deal was essentially master-minded by, and benefited from the unconditional support of, the highest levels of the Chinese government.[29]

Rather, the "sinophobia" argument offers a much more compelling argument for strong U.S. opposition. And though it is easy to dismiss such reactions as a mere replay of the perceived "Japan Threat" of the 1980s, one has to acknowledge striking differences between Sinophobia of the 21st century and Japanphobia of the 1980s; differences that, indeed, give the vehement manifestations of the former an certain air of legitimacy. Not only is there no George-Jintao relationship that can even remotely approach the Ron-Yasu (Ronald Reagan-Yasuhiro Nakasone) friendship, but the Chinese dragon is not comfortably nested in the Allied camp. The Chinese may well prove more successful in the long-term in purchasing icons of American corporate power than the Japanese have ever been.

Arguably, Lenovo's acquisition of IBM's PC division in December 2004 and the failed Haier bid for Maytag may only be the beginning of a Chinese corporate offensive. Viewed in this light, political opposition to the CNOOC bid takes on a new dimension entirely. National security concerns surrounding the proposed merger were certainly not based on thin air; yet, neither were they as pronounced as the political rhetoric coming out of the U.S. Congress suggested. Indeed, to the extent that one may be tempted to buy into the assertion that the CNOOC bid was nothing more than a politically motivated and calculated move by the Chinese government – a move potentially designed to lay the foundation for China credibly rivaling the U.S. on the world stage – so, too, one cannot ignore the fact that Congressional opposition was driven more by political motivations than economic fundamentals.

Former Federal Reserve Chairman Alan Greenspan and then-U.S. Treasury Secretary John W. Snow called for moderation amid near-immediate calls for retaliation once the unsolicited bid had been announced. Moreover, they cautioned against giving in to emotional and politically-motivated impulses for punitive legislation on the grounds that they could lead both countries down the road of an all-out trade war, which could eventually prove most detrimental to the U.S. economy.[30] Yet, as evidence produced below will show, in their determination to block the CNOOC takeover of Unocal, politicians did not shy away from playing the national security card above and beyond objectively justifiable levels. In the process, information that would have been relevant to a balanced assessment has been conveniently omitted, while other facts have been purposely distorted. Considering the overall context in which the CNOOC bid took place, political motivations have significantly informed the debate on the U.S. side, and thus precluded an objective, balanced assessment of the CNOOC bid. It remains to be seen if the outcome will indeed yield the result that lawmakers intended – safeguarding U.S. national security interests. The verdict on that is likely to be at best a mixed one.[31]

Underlying the heated CNOOC debate was a bitter slice of irony: pressure for Chinese currency revaluation. Revaluation of the Chinese yuan, as the U.S. consistently pushed for at every possible occasion, will only result in increasing Chinese companies' ability to buy U.S. firms; a consideration that is obviously lost on overzealous politicians that are simply eager to ride the wave of China bashers. The Chinese may well bow to growing U.S. pressure in the end, although the extent to which they do will be according to their own timetable. And if they do, the U.S. may well get the outcome it wants; the question, however, will be whether the administration will like what it is going to get. Considering that the irony lies in the fact that currency revaluation will make it even easier for Chinese corporations to buy foreign companies, that answer would decidedly be NO!

It was, of course, inevitable that the CNOOC bid conjured up national security concerns that to some extent certainly would have warranted careful and diligent scrutiny. However, the nature and dynamics of U.S. opposition to the deal appears to have been driven almost exclusively by national security and political considerations, with scant attention to economic analysis. Indeed, though analysts did not dispute the legitimacy of requesting a substantive review of the CNOOC bid on national security grounds, there was a widespread consensus that a CNOOC-Unocal deal would almost certainly have passed an objective national security test. Arguably, a most basic level of objectivity would include an attempt to achieve a proper balance between economic and national security considerations, especially in light of CNOOC's stated willingness to offer wide-ranging concessions to placate overt security concerns. If anything, pundits supportive of the deal maintained, "China's purchase of Unocal could have meant more investment in global oil exploration and drilling than Unocal or other American companies have been willing to make."[32]

Hard-nosed, purely economic considerations also run the danger of over-simplifying a complex transaction, to the extent that relevant national security concerns are marginalized. Nevertheless, it is equally hard to refute some of the economic arguments in favor of the proposed merger. The Chinese press was quick to point out the sharp contrast between noted economists and Washington politicians on this matter. Where some economists saw a potential for an inclusion of capital and new markets, others saw Chinese buy-outs of foreign companies as an optimal incentive for China to seek better trade relations, given that it "turns them into a stakeholder."[33]

On a broader economic level of analysis, the economics of China bashing are dismissed as lacking compelling evidence and rationality.[34] Attempted takeovers of U.S. commercial entities by Chinese companies are beginning to spread unease about China's rise as a major financial player. Yet, what about the equally palpable reality that Chinese buy-outs pose significantly fewer risks than does growing accumulation of United States Treasury Bonds, which can be much more easily divested than large-scale investment in U.S. companies? The hypocrisy of U.S. motives to oppose the CNOOC bid was most aptly summarized in the sarcastic note that when Chinese companies aim to diversify their dollar holdings and attempt to buy major stakes in foreign companies, they are demonized as corporate vehicles of a Communist dictatorship, whereas they are deemed acceptable when buying U.S. debt.[35]

In an overzealous attempt to substantiate his opposition to the CNOOC-Unocal deal, Sen. Charles Schumer (D-NY) produced a sound bite that, upon close scrutiny, ought to have undermined the very effect he intended. "Does anybody honestly believe that the Chinese would let an American company take over a Chinese company?" he famously quipped in the U.S. Senate. Apparently, little did he (and his staff) know that the Chinese government had already given the green light to just such a commercial activity in 2004. Apart from U.S.-based Anheuser-Busch buying Harbin Brewery Group, one of China's largest and oldest beer makers, Procter & Gamble hit the M&A jackpot in China in 2004 when it succeeded in buying out Hutchison Whampoa. In fact, the merger & acquisitions (M&A) market in China ranks among the world's most promising.[36]

Though it is entirely possible that ignorance of the facts can, as in Senator Schumer's case, convincingly be attributed to political expediency, it is much more difficult to offer similar excuses for excessive misrepresentation of facts by Richard D'Amato, Chairman of the U.S.-China Economic and Security Review Commission (USCESRC). In a July 13 statement, D'Amato argued that "China has also attempted to persuade Russia to route a pipeline from Siberia directly to China, rather than to the Pacific port of Nakhoda, where the oil would be available to the world market."[37] Absent further contextualization, the statement reads as though the Chinese government was actively trying to persuade Russia from abandoning the planned Angarsk pipeline route to Nakhoda, which could not have been further from the truth.

In fact, the pipeline route is still set to go to the Siberian Pacific Coast city of Nakhoda in order to serve the Japanese market rather than the world market at large, as argued by D'Amato. The Chinese government has merely succeeded in securing Russia's commitment to prioritize the building of a Chinese branch pipeline. While China's interest in Russian oil sources is undeniable, the Russian government's drawn-out deliberations over the Angarsk pipeline rested on the difficulty of balancing strategic flexibility (focusing on China) with economic profitability (Japan and South Korea).[38] It is indeed interesting to note that, prior to CNOOC's bid for Unocal, the Angarsk pipeline project barely raised an eyebrow among members of USCESRC.

Furthermore, arguing that the CNOOC bid "simply is not a market-based transaction" because "China is not a market economy"[39] shows the determination of the U.S. side to discredit the bid on even the most perfunctory grounds. Above all, it reveals the pervasive weakness of the U.S. argument, and it elucidates the glaring absence of any coherent China strategy, above and beyond alarming and overblown rhetoric.

All the while insisting on the purely commercial nature of the proposed transaction, CNOOC top management also acknowledged some of the more relevant national security concerns that would certainly prevent any deal from being concluded. Hoping to alleviate pressing U.S. concerns, CNOOC announced a range of concessions to address security concerns and insist on the exclusive business aspect of the transaction. The proposed concessions, however, remained conveniently unacknowledged in the CNOOC-Unocal debate in U.S. policymaking circles.

A somewhat more credible charge leveled against CNOOC centered on the notion of unfair trade practice. Specifically, CNOOC's heavily subsidized loan package[40] invited calls of unfair trade practices and raised questions as to the Chinese government's intention in underwriting much of the deal. In the words of the chairman of USCESRC, "the U.S. government should see and treat this proposed transaction as a non-commercial transaction with other motivations and purposes."[41] Responding to the allegations of unfair trade practices, the Chinese side was quick to point out that the United States did not oppose Chinese purchase and present holding of US$ 230 billion of United States Treasury Bonds, transactions that have repeatedly been facilitated by continuous subsidies.[42]

In addition, the CNOOC bid was instrumental in putting the Committee of Foreign Investment in the United States (CFIUS) under intense scrutiny. The U.S.-China Economic and Security Review Commission (USCESRC) seized the opportunity to lament serious flaws in the CFIUS statute. In the eyes of its critics, the membership expansion of CFIUS over time – it grew from four members at the time of its creation to twelve at present – has resulted in a loss of focus. Most importantly, these pundits argue that having this interagency group led by the U.S. Department of the Treasury effectively hampers prioritization of national security considerations. In light of the CNOOC bid, there have been renewed calls to replace this "fox guarding the chicken coop" with a federal department that would be much more favorably disposed to bringing national security mindedness to CFIUS deliberations.[43]

In the end, the attempt at amending and/or replacing the current CFIUS process played a significant role in CNOOC's decision to abandon its bid on August 2. In a press release, CNOOC noted that it had

"…given active consideration to further improving the terms of its offer, and would have done so but for the political environment in the U.S. The unprecedented political opposition that followed the announcement of our proposed transaction, attempting to replace or amend the CFIUS process that has been successfully in operation for decades, was regrettable and unjustified. This is especially the case in light of CNOOC's purely commercial objectives and the extensive commitments that CNOOC was prepared to make to address any legitimate concerns U.S. regulators may have had regarding our acquisition…."[44]

Implications for the Future

China's omni-directional and diversified oil investments have for several years been a major subject of concern in various policy circles in the United States. The leading proponent of growing national security challenges related to China's global oil diplomacy has been the U.S.-China Economic and Security Review Commission (USCESRC). In annual reports delivered to the U.S. Congress, USCESRC has offered critical assessments on China's oil investments and raised concerns over China's apparent arms deals in the Persian Gulf region.[45]

In the wake of the withdrawal of the CNOOC bid, The Economist provided a sobering assessment of the potential short- to long-term ramification(s) of the outcome. It noted that "by denying China access to energy assets through legitimate means, America might expose itself to bigger threats."[46] In other words, the erection of a protectionist wall manned by national-security proponents may ironically result in nothing more than a gradual weakening of that very security. Protectionism might also result in an increase in activities that USCESRC has been raising alarm about, most notably highly politicized bilateral energy ties between China and countries such as Angola, Nigeria, Iran, Sudan and Kazakhstan.

Thus, in the short-term, the recent American manifestation of protectionist capitalism is likely to further embolden the Chinese in their search for alternative oil investment opportunities. The immediate results are likely to be highly disconcerting to any U.S. administration. Take for example, China's expanding relationship with Iran, which is currently China's second-largest oil supplier. Not only is Iran well positioned to alleviate China's thirst for oil, but the country's growing appetite for consumer goods can be easily served by China's burgeoning manufacturing industry. Though arms sales to the Middle East are still a lucrative business, China has significantly expanded its non-petroleum business ventures in Iran. The thinking is that a general willingness to invest in the country will go a long way toward securing oil supplies over the long-term.[47] And judging from the words of Bijan Namdar Zanganeh, Iran's Oil Minister, China has been quite successful thus far in wooing Iran. In comments made during a visit to China in late 2004, he noted that "Japan is our number one energy importer due to historical reasons ... but we would like to give preference to exports to China… From the supply side, we have no difficulties (in making China the top energy oil importer from Iran)."[48]

The deepening Sino-Iranian relationship, however, has also caught Washington's attention in recent years. Sino-Iranian ties have important geo-strategic and geo-political repercussions because, on the one hand, these bilateral ties give rise to weapons proliferation concerns. China is widely suspected of channeling ballistic-missile components, as well as air-, land-, and sea-based cruise missiles to Tehran, in addition to crucial assistance in its nuclear development program.[49] On the other hand, enhanced Sino-Iranian ties could also seriously complicate U.S. strategic and security plans.[50] Indicative of such political roadblocks has been China's strong opposition earlier this year to having the Iranian nuclear issue referred to the United Nations Security Council.

In addition, the Sudan features prominently in China's overall oil import equation, accounting for some six percent of total Chinese oil imports. As such, China has important strategic interests in Sudan, which serves as its supply chain center in Africa. Thus, it comes as hardly a surprise that China has been reluctant to endorse a recent UN resolution over perceived acts of genocide in Darfur for fear of losing its influence over the country's oil reserves and, in the case of a subsequent regime change, seeing these resources become accessible to Western oil interests.[51]

Conclusion

Ultimately, in the face of a rising China, it is imperative to finally draft a China strategy that is based on sound and balanced assessments rather than over deterministic, one-sided and ill-informed analyses of China. If the executive and legislative branches of the U.S. government continue to leave the China debate to pseudo-China bashers and security hawks, it may encourage exactly the opposite of what it intends. Blindly clinging to neo-realist, rational choice interpretations of China's outward oil-economy and increasingly assertive foreign policy will result in an institutionalization of ill-informed, biased, and unfounded assessments that will lead to further ossification of what is already a hopelessly inappropriate China strategy.

Contrary to stated arguments that U.S. policies toward China have been, and continue to be, dominated largely by narrow commercial concerns,[52] I maintain that the CNOOC case is one of the most concrete examples yet of "bogus fears and hidden interests"[53] driving policy decision-making towards China. The policy dilemma that underlies much of the heated reaction to the CNOOC bid is the perennial question of how to deal with a rising and ever more economically powerful China. Is China to be truly put into the "rival" camp or be welcomed as a partner? Taking stock of the current geo-economic and geo-political reality, political and economic return on investment is going to be most attractive by subscribing to the latter approach.

Ultimately, it boils down to an intricate cost-benefit analysis. The choice of approach will significantly determine the extent to which China can be 'guided' along the political and economic growth path on terms most appealing and beneficial to the U.S. Contrary to widespread perception in policy-making circles in the United States, U.S.-China economic relations in general, and Chinese merger/acquisition attempts in particular, do not connote a zero-sum game. However, replays of politically motivated actions as were evident in the recent case provide fertile grounds for outcomes that most decidedly will not be in the best interests of the United States, whether economic, national security or diplomatic.

Chinese MNCs are making credible, and at times risky, advances into the global marketplace.[54] Whether or not this presents a welcome development for particular political and/or business interests – not just in the United States but worldwide – it is a reality that cannot be ignored, wished away, or warded off with protectionist measures in the medium- to long-term.[55] The real question is: What is an appropriate China strategy in the age of Chinese MNCs? How and to what extent does the current China strategy have to be revised so as to fit the new reality?

The failed CNOOC bid offers policymakers plenty of tea leaves to read. One thing, however, is certain: discarding free market rhetoric for protectionist impulses – except for immediate and substantiated national security arguments – is a fail-safe political mechanism to have China emerge truly as a rival in the global marketplace, with all the geo-economic and geo-strategic implications. Better to co-opt China into greater global integration with a few sacrifices than to trumpet short-term success in thwarting Chinese corporate takeover efforts at the expense of medium- to long-term adverse outcomes. The sad reality, though, is that most of the China-bashing political crowd of Washington D.C. is unaware of the futility, and indeed the counterproductive effect, of their current policy stance and flawed China strategy. In other words, Washington is badly in need of a fundamental and coherent review of its strategic assessment of China.

ENDNOTES

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