CHINA'S NEW COURTSHIP IN SOUTH SUDAN

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EXECUTIVE SUMMARY AND RECOMMENDATIONS

In the wake of Sudan's partition, Beijing has accelerated a re-orientation of its engagement in the resulting two states, most significantly through a new courtship in Juba. China's historical support for Khartoum left a sour legacy in the South, but the potential for mutual economic benefit means a new chapter in bilateral relations is now being written. Balancing new friends in Juba with old friends in Khartoum, however, has proven a delicate dance. China has been drawn into a high-stakes oil crisis between the two, the consequences of which may temper an otherwise rapidly expanding relationship with Juba. A sustainable solution to the crisis cannot be achieved in isolation; North-South stability, mutual economic viability and the security of Chinese interests will also depend on answers to other unresolved political and security issues, including in Sudan's marginalised peripheries. The future of Beijing's dual engagement, and the kind of relationship that emerges in the South, will depend in part on how the oil standoff – and this broader reform agenda – are confronted.

As South Sudan prepared for its 2011 self-determination referendum, China recognised the increasing inevitability of independence. Eager to maintain stable relationships and the continuity of its oil investments – now situated primarily in the South – its stance evolved to reflect changing political realities. Beijing is keen to preserve and expand its footprint in South Sudan's oil sector, but Chinese companies are also flocking to other sectors, above all to build infrastructure in a country that has almost none.

China's cultivation of new political and economic relations has been most visible in the surge of bilateral exchanges with Juba over the last year, which is expected to be capped in the coming weeks by President Salva Kiir's first visit to Beijing as head of state. As they seek to build bridges with the South, the Chinese are keen to draw comparisons with their own experience of economic transformation and rapid rural development, as well as to emphasise a sense of shared historical experience at the hands of imperial powers.

South Sudan is very much "open for business", actively seeking foreign direct investment from West, East, and everywhere in between. Historical ties may be strongest with the West, but Juba has made clear that if the Chinese are first to come and partner in developing the new nation, they will not hesitate to welcome them. Furthermore, China's "no strings attached" political approach and economic cooperation model is as attractive in Juba as it has proven elsewhere on the continent, not least in resource-rich states eager to develop fast.

As Juba opens up to new investment, it should take two critical factors into consideration. First are potential correlations between the economic partnerships it forges, the character of the state that emerges and its foreign policy. While it hopes to remain politically aligned with the West, time will tell whether expanding economic partnerships with China or others will have a gravitational effect. For now, it wants to welcome, and leverage, the interest of all actors.

Secondly, in the midst of a mounting budget crisis, Juba must consider how to secure and direct investment so as to best serve its development agenda, calm its own domestic insecurity and prevent even greater state fragility. It must actively shape new economic relationships rather than become a passive recipient of foreign-authored investment. Given limited government capacity and an untested legislative framework, its economic planners must take care to harness such investment for its own benefit, lest Africa's newest state be overrun in a resource scramble.

The number of Chinese nationals and commercial actors in Juba has spiked dramatically in the nine months since independence. Beyond oil, Chinese companies are most interested in infrastructure, and South Sudan needs everything: roads, bridges, telecommunications, power plants, electricity grids, schools, hospitals, municipal buildings, water treatment facilities, dams and irrigation systems and new oil infrastructure. Companies are registering, conducting feasibility studies, and drafting proposals, but major deals are yet to be landed. Though China's central government often plays a role in helping secure market access, Chinese engagement in South Sudan is not monolithic. Private businesses and small-scale entrepreneurs are driving new investment as much as the state.

Some of Juba's elite remain hesitant about putting too many eggs in one basket, and even those most eager to secure a major economic partnership argue there will be no Chinese monopoly. Beijing affirmed in January 2012 its intent to offer an economic package, including development grants and a possible billion-dollar infrastructure loan, and details are being negotiated. But new uncertainty over the future of Juba's oil sector and continued North-South instability have altered the equation and may reduce the total offered in the end. Given the greater variety of financing opportunities now available to Beijing's government "policy" banks and thus an increased sensitivity to risk, the scale of a loan may not match those extended to other resource-rich African states. Chinese companies will actively pursue contracts in any case, though most would prefer the loan financing that normally ties contracts to Chinese firms.

The budding bilateral relationship has strained of late, as Beijing has been drawn uncomfortably into the oil dispute between North and South. An African Union (AU) team, backed by the UN and other partners, continues to facilitate talks between the parties. Tense negotiations on security, borders, citizenship, financial arrangement and the export of oil have yet to yield concrete agreements and are complicated by ongoing conflict in Sudan's border states. The impasse led to a shutdown of the oil sector in early 2012 that has imperilled both economies and prompted renewed war rhetoric. Most remaining oil is now in the South, but the predominantly Chinese-built infrastructure to exploit it – pipelines, refinery and export terminal – is in the North. Given comparatively modest proven reserves, oil imports, whether from North or South, no longer occupy the significant position in China's global energy strategy they once did. But given the considerable investment in developing and operating the oil sector, the Sudans remain important for China National Petroleum Company (CNPC), the state-owned oil giant, and thus a focus for the government.

As negotiations toward a North-South oil deal foundered dangerously in late 2011, the role of China came centre stage, and many in the international community (and in the two Sudans) thought Beijing would be forced to intervene. Juba wanted help in pressuring Khartoum to cut a reasonable deal, and when the North began to confiscate Southern oil instead, it interpreted China's inaction as passive complicity and moved to leverage its increasingly uncomfortable position.

At the same time, Chinese-led oil consortia were engaged in their own set of negotiations with Juba over the transition of oil contracts previously held by Khartoum. The financial terms were retained, but significant changes were made to strengthen previously neglected social, environmental, and employment standards. In light of the heated row with Khartoum, Juba also bargained hard to include measures that would bring oil company interests in line with its own and secure considerable legal rights and compensatory protections in the event of an oil-sector shutdown. It also secured discretion over the post-shutdown extension of contracts based on, among other things, companies' cooperation in helping resolve the impasse with Khartoum. The interplay between the parallel negotiations added another dimension to China's increasingly complicated position.

Both sides, as well as many international actors, assumed China would weigh in more assertively, though perceptions of Beijing's influence and readiness to employ it were unrealistic. The shutdown of the oil fields, abduction of Chinese construction workers in Southern Kordofan and expulsion of the head of a Chinese-led oil consortium added to Beijing's vexing political problem and generated anxiety among Chinese nationals in North and South. Both Sudans continue to try to pull China into their respective corners, but Beijing has resisted taking sides, as its principal objective remains balanced relations with North and South.

That said, many – including in Beijing – argue China can and should do more to ensure peaceful resolution, without compromising its interests or traditional adherence to a principle of non-interference. A recent shift in the North-South negotiation presents a possible new entry point for the international community, including opportunities for China to help break the deadlock, ease its own position and bolster stability within and between the two states. Beijing has shown signs of new engagement in recent weeks, but the comparatively weak domestic status and limited resources afforded to the foreign ministry must also be considered. China's diplomatic capacity does not always reflect the powerful position the country enjoys on the world stage.

The oil impasse may temper the pace of Chinese engagement in the South but is unlikely to stall it. Angered by its sense that China still "treats it as a province rather than an independent state", Juba will continue to make demands, particularly with regard to management of its oil sector. But if managed pragmatically, the opportunities for mutual economic benefit should trump episodic tensions. China's new expedition in the South and its attempt to balance relations with the two Sudans have proven tricky tasks, however, that will continue to challenge the boundaries of its foreign policy.

RECOMMENDATIONS

To the Government of South Sudan:

1. Manage relations with China so as to pursue legitimate near-term demands in the oil sector without endangering the broader political and economic relationship.
2. Articulate to Beijing a detailed set of priority projects for loan financing based on an assessment of current

financial constraints, future debt burden, projected oil revenue and other donor commitments; harmonise the inputs and experience of Juba's traditional development partners with the comparative advantages of Chinese entities in a way that best serves South Sudan's development agenda.

3. Formalise an economic task force to consider the country's investment strategy and partnerships and their effect on national development and foreign policy.

4. Harness new foreign investment, including by:

   a) ensuring transparency and cost efficiency through competitive bidding;

   b) setting clear social, environmental, and quality standards; and

   c) negotiating training and employment targets for both skilled and non-skilled positions so as to maximise employment of South Sudanese nationals.

To the Government of China:

5. Assume political responsibilities commensurate with economic status by:

   a) building on recent diplomatic efforts through more active and regular involvement in the North-South negotiations, including by directly engaging, via an empowered special envoy, the parties in support of African Union (AU) efforts to secure an agreement on the export of oil, as well as other outstanding political and security issues;

   b) offering financial assistance to help cover a portion of Khartoum's coming revenue gap, per the AU proposal, in combination with Juba's proposed contribution and necessary austerity measures in the North. Given the need for considerable restructuring in Khartoum's flawed economic model, such funds may best be administered in conjunction with an internationally-monitored program and guided toward smoothing the fiscal transition; promoting productive sectors beyond oil; and fostering greater economic decentralisation; and

   c) recognising, given the interconnected nature of security between Sudan and South Sudan, that financial assistance alone will not yield a sustainable solution. Continued instability along the shared border and in Sudan's marginalised peripheries will remain a threat to peace and to mutual economic viability, as well as to Chinese interests in both. Credible progress on these fronts must accompany financial assistance, or the money will be wasted.

6. Consolidate relations with Juba and protect the security of Chinese investments by ensuring Chinese companies in South Sudan exercise good business practices; place emphasis on areas that have hurt China's reputation in the past, notably transparency, social and environmental considerations, local employment targets and quality delivery; and improve China's standing by ensuring the benefits of commercial engagement and partnerships extend beyond government elites.

7. Extend a preferential loan package from the Chinese Export-Import (Exim) Bank – in coordination with other creditors – to support development of South Sudan's infrastructure, so as to aid in opening up non-revenue sectors.

Juba/Beijing/Nairobi/Brussels, 4 April 2012

CHINA'S NEW COURTSHIP IN SOUTH SUDAN

I. INTRODUCTION

Narratives of China and Sudan have historically reflected the nature of the two countries' engagement – focusing almost exclusively on relations between Beijing and Khartoum. In the wake of Sudan's division, this report aims to shed light on the new and rapidly evolving political and economic relationship between China and the Republic of South Sudan, while also addressing the challenges Beijing confronts in re-orienting relations with partners in both North and South. Primary research was conducted in Juba, complemented by research in Beijing, Shanghai, Addis Ababa and Washington between November 2011 and February 2012.

This report first reviews the evolution of Chinese policy on South Sudan and recent expansion of relations between the two. It then explores their mutual interest in economic cooperation and depicts the growing presence of Chinese businesses in infrastructure and other commercial sectors. Finally, it reviews the role of oil as a centrepiece in relations with China, as well as a source of conflict: first by detailing the transition of Chinese-led oil consortiums from North to South, and then through an analysis of the uncomfortable position in which China now finds itself, drawn into an oil crisis and heightening war rhetoric between Sudan and South Sudan.

II. A NEW COURTSHIP IN SOUTH SUDAN

Independence has created new political realities in the two Sudans, and China has responded accordingly. A new strategic courtship has followed the oil south, and while Beijing's relationship with Juba is evolving fast, and the future may be bright, the transition has proven a delicate balancing act. Because Beijing's relationship with Sudan was previously channelled almost exclusively through Khartoum and its ruling National Congress Party (NCP), it has had to build a relationship in the South, particularly with the ruling Sudan Peoples' Liberation Movement (SPLM), from the ground up, while reassuring Khartoum that it has no intention of leaving old friends behind. This re-orientation continues amid still hostile relations between North and South, frequently drawing China into uncomfortable positions.

Cognisant of, and uneasy about, historically negative perceptions of China in the South, Beijing's new strategy reflects a desire to focus not on the past but on opportunities for mutual benefit ahead.[1] This has been most visible through the steady increase in diplomatic, party, business and other exchanges between Beijing and Juba that first followed the 2005 Comprehensive Peace Agreement (CPA) that ended the civil war, but became far more frequent in advance of, and immediately after, South Sudan's independence in July 2011.[2] Party-to-party relations, long an important conduit between Beijing and Khartoum, now occupy a similar role in the liaison with Juba.[3]

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[1] A Chinese national felt that the South Sudanese were open to cooperation but remained wary "in their hearts". Crisis Group interview, Juba, November 2011.
[2] See text boxes below on pre- and post-independence "Bilateral Exchanges Between Beijing and Juba".
[3] South Sudan's current political structure – in which state and party are sometimes indivisible – is not altogether dissimilar to that in Beijing. While Western governments and NGOs have long been working with the SPLM to advance democratic ideals in line with Juba's stated aspirations, a Communist Party of China (CPC)-SPLM dialogue, exchanges of national party officials, and training of SPLM national and state party officials in China offers exposure to an alternative model.

Most recent visits have focused on promising opportunities for cooperation, but political messages are often delivered as well. Given China's early, and considerable, reservations about the partition of Sudan, the South's semi-autonomous government first petitioned Beijing to accept the self-determination referendum and its outcome. Once independence was realised, the new state sought Beijing's help in pressuring Khartoum on contested North-South issues – most notably on oil and transitional financial arrangements. Chinese counterparts meanwhile encouraged restraint, peaceful negotiation, and stability, not least due to concerns over the security of their investments.

China's primary interest in South Sudan is, without question, oil and other commercial investments. But its engagement is not driven solely by its voracious resource appetite. China has cultivated diplomatic relationships in Africa to serve political objectives as well, namely to strengthen its political alliances and networks in international institutions (eg, the UN and the World Trade Organisation), to "emphasise sovereignty as a core foreign policy principle" in the international arena,[4] and to buttress international support for its "One-China" policy. In South Sudan however, these motives are at best complementary to economic pursuits. [5]

A. China in Sudan: Historic Relations and Southern Perceptions

China established relations with Sudan in 1959, and though ties grew in the ensuing decades, the development of the oil sector in the 1990s, the economic partnership it catalysed and the geopolitical environment in which it occurred marked a new and historically significant era.[6] When Sudan's National Islamic Front (now the NCP) seized power in 1989, its ideological agenda and links to terrorism quickly led to international isolation and, ultimately, unilateral U.S. economic sanctions. As a result of deteriorating relationships abroad, and pressure from the West in particular, the regime looked to China to develop its oil sector and found a willing partner.[7] Though an unstable investment climate, the relative economic isolation meant China enjoyed a particularly favourable entry into a largely untapped oil market. Other Chinese enterprises followed, and the alliance with Sudan took on greater importance.

The development of the oil sector – and by extension China's role in it – was marred by its direct link to the country's brutal civil war (1983-2005), which was fought largely in the South. Though that conflict had begun years earlier, the Chinese-facilitated oil boom came to fuel Khartoum's war economy, pay for its armaments and consequently be associated among Southerners with forced displacement, social devastation, gross human rights violations and unchecked environmental damage.[8] Later, it was widely suspected that the oil companies were complicit in Khartoum's manipulation of production figures and revenue.[9]

Throughout that period, Khartoum tightly controlled relations with China from the centre, largely preventing its ally from having contact with the Southern rebels.[10] Beijing reciprocated by dealing almost exclusively with the central government. Attempts to paint this stance as a reflection of China's principle of "non-interference" in the affairs of sovereign nations are seen as disingenuous by many Southerners, given the undeniable national implications that were generated by the economic intervention of

[4] Deborah Brautigam, professor of international development and China-Africa expert, "Remarks before the Senate Committee on Foreign Relations Subcommittee on African Affairs" Washington DC, November 2011.
[5] Crisis Group interviews, foreign policy experts, Beijing, February 2012, China-Africa experts, Washington DC, December 2011.
[6] Daniel Large, "Sudan's foreign relations with Asia: China and the politics of looking East", Institute for Security Studies (ISS), no. 158 (2008).
[7] Other Asian firms also invested heavily in the sector, mostnotably the Malaysian state-owned oil and gas company Petronas.
[8] For a detailed account of these issues, as well as the role of oil development (including oil company complicity) as a driver of conflict, see: Crisis Group Africa Report N°179, *South Sudan: Compounding Instability in Unity State*, 17 October 2011; "Sudan, Oil, and Human Rights", Human Rights Watch, 23 November 2003; John Harker, *Human security in Sudan: the report of a Canadian assessment mission* (Ottawa, 2000); Georgette Gagnon, John Ryle, "Report of an Investigation into Oil Development, Conflict and Displacement in Western Upper Nile, Sudan", www.sudanarchive.net, October 2001; Crisis Group Africa Report N°39, *God, Oil, and Country: Changing the Logic of War*, 28 January 2002. For more information on China's oil investments in Sudan and their impact on the conflict in Darfur, see also Crisis Group Asia Report N°153, *China's Thirst for Oil*, 9 June 2008.
[9] Such mistrust was rekindled following the January 2012 shutdown of South Sudan's oil sector. See Section V below for details.
[10] Khartoum actively worked to curtail Beijing's contact with the South and control Chinese perceptions of domestic political dynamics, first during the war but also after the signing of the CPA. SPLM officials report that during the war, with the help of friends elsewhere in Africa, they reached out to Beijing through Chinese embassies on the continent, complaining of the effects of their relationship with Khartoum and lobbying them to change course. Associations were often made between Taiwan and South Sudan. Southern officials occupying posts in Sudan's CPA-era Government of National Unity report they were often intentionally left out of official functions involving the Chinese. Crisis Group interviews, cabinet ministers, Juba, November 2011.

China and its oil companies, as well as the sale of arms.[11] Opponents of Khartoum were further incensed by China's shielding of the regime internationally (most notably at the UN Security Council).[12] Anger toward China did not die with the end of the civil war. The perception in the South was that Beijing had underwritten an autocratic regime, helped facilitate the devastation and economic exploitation of the South and aided in preserving the country's fundamental centre-periphery problem.

The 2005 CPA outlined a new political dispensation, including by granting greater autonomy to a regional government in the South. It also extended to Southerners a right to exercise self-determination at the end of the CPA period in 2011,[13] though the agreement's primary aim was to "make unity attractive" in the interim. That was an objective that squared with Beijing's preference for unity in Sudan and its foreign policy goals more broadly. But before long, persistent North-South acrimony and failures in CPA implementation cast a shadow over that prospect.

B. The Turning Point: Salva Kiir Visits China

Though the SPLM began to engage China during the CPA period (first through a 2005 Salva Kiir visit to Beijing), progress in building relations was slow. It was his second visit, in 2007, that today is regarded in Juba as the "real beginning" of bilateral relations.[14] Because he then held dual titles as first-vice president of Sudan and president of the regional southern government, this visit was "official", and Kiir was flanked by Northern and Southern officials from the national and regional governments.[15] Though talks were wide-ranging, an individual familiar with the visit summarised the principal message to Beijing as follows: "Kiir and company brought a copy of the oil map and a copy of the CPA's Machakos protocol guaranteeing the South's right to secede. He put the two documents on the table and said, 'you figure it out'".[16] This visit – and the message delivered – marked a turning point in Chinese policy on Sudan.[17]

China began to respond, opening a consulate in Juba in September 2008 with a staff of three. Public and private engagement began to grow, though the Chinese took great care to manage the unhappy rumblings from their partners in Khartoum.[18] As the CPA period entered its final stretch, Beijing pursued a "hedging strategy geared toward the possibility of Southern secession, and then began to quietly but actively prepare for this inevitability".[19] Though its reservations about separation remained, the referendum had broad international backing and the likely outcome was clear. Pragmatism demanded both evolution of its public messaging on self-determination and amplification of political, economic, and party interaction with Juba and the ruling SPLM.[20] The 2007 visit laid bare the centrality of oil in the shifting dynamics between China and the two Sudans. The potential division of the oil sector –

[11] Crisis Group interviews, South Sudanese government and military officials, Juba, November 2011, China-Africa expert, Nairobi, December 2011.

[12] This was exhibited not only with regard to the South, but also later over Darfur, another of Sudan's marginalised peripheries. In 2006 and again in 2010, UN panel of experts reports noted that Chinese-made weapons, ammunition, and other materiel continued to be transferred by Khartoum to state and non-state actors in Darfur in breach of the arms embargo imposed by UN Security Council Resolution 1556. The resolution prohibits arms transfer to Darfur, not to Khartoum. Some states have stopped sales to Sudan since they cannot control where the weapons will be used. Those that continue to supply arms to Khartoum maintain it is the government's responsibility to comply with the UN arms embargo. For further analysis on Darfur, see Crisis Group Africa Reports N°134, *Darfur's New Security Reality*, 26 November 2007; and N°152, *Sudan: Justice, Peace and the ICC*, 17 July 2009; and Africa Briefing N°72, *Rigged Elections in Darfur and the Consequences of a Probable NCP Victory in Sudan*, 30 March 2010.

[13] The CPA's six-year interim period began in July 2005, during which CPA provisions were to be jointly implemented through the "one country, two systems" structure. While the agreement aspired to "make unity attractive" between North and South, it also mandated a right for Southerners to vote in a self-determination referendum six months before the end of the interim period in July 2011.

[14] Crisis Group interviews, senior SPLM members, Juba, November 2011.

[15] The delegation also included current Information Minister Baranaba Marial Benjamin and Cabinet Affairs Minister Deng Alor, senior SPLM figure Luka Biong, current SPLM-Democratic Change (SPLM-DC) Chairman Lam Akol, and other national ministers from the central government in Khartoum. At the time of his first visit, in 2005, Kiir was deputy commander of the rebel Sudan Peoples' Liberation Army (SPLA).

[16] Crisis Group interview, international official, Juba, 2009.

[17] Meanwhile, Southern officials in Khartoum, particularly those working in the oil sector, began to hint to Chinese oil representatives what was coming. Crisis Group interviews, Juba, November 2011. For a detailed history of the evolution of China's public and private relationships over the course of the CPA period, see Daniel Large, "South Sudan and China: 'turning enemies into friends'?", in Daniel Large and Luke A. Patey (eds.), *Sudan Looks East: China, India, and the Politics of Asian Alternatives* (Oxford, 2011), pp. 273-288.

[18] Crisis Group interviews, SPLM member, Sudan expert, Juba, November 2011.

[19] Ibid; Daniel Large, "South Sudan and China: turning enemies into friends?", in *Sudan Looks East*, op. cit., p. 273.

[20] Meanwhile, given that secession appeared inevitable, Chinese officials also lobbied Khartoum to maintain stability by facilitating and accepting a peaceful referendum, including during the Sudanese foreign minister's September 2010 visit to Beijing.

and the associated political and economic complications – was now a time-bound fixture on the horizon. In the absence of sufficient contingency planning in the run-up to separation, the die of China's current entanglement would soon be cast.

C. Independence: A New Beginning

South Sudan achieved independence on 9 July 2011. President Hu Jintao's representative to independence day ceremonies, Jiang Weixin, signed a joint communiqué with Southern officials recognising the new state, establishing diplomatic relations and upgrading China's consulate to an embassy.[21] Foreign Minister Yang Jiechi soon visited Juba and bilateral exchanges increased in frequency. Though China's historical support to Khartoum means a lingering uneasiness remains in the South, the prevailing sentiment today among government elites is "there are no permanent enemies".[22] Juba is taking a pragmatic view, looking not to the past but to the huge role China could play in trade and development.

As they seek to build bridges (and set themselves apart from the West), the Chinese are keen to emphasise a sense of shared historical experience at the hands of imperial powers and to draw comparisons with their own process of economic transformation and rapid rural development. The exposure to China also offers the South an alternative example of the role of the state in development. How relevant China's domestic experience will prove to be for Juba remains to be seen, as some see it as merely a means to heighten its appeal.[23] Chinese officials are also quick to note that this is not their country's first engagement in the South, recalling the medical teams that were dispatched beginning in the early 1970s, a form of foreign aid deployed to many African states. Some 340 Chinese medical staff earned positive reviews for their work at centres in Juba, Wau, and Malakal until they exited when the civil war began.[24]

During his first official visit, Foreign Minister Yang Jiechi indicated the same "Five Principles of Peaceful Coexistence" that guide Chinese foreign policy elsewhere will frame the relationship with South Sudan: 1) mutual respect for sovereignty and territorial integrity; 2) mutual non-aggression; 3) mutual non-interference in internal affairs; 4) equality and mutual benefit; and 5) peaceful co-existence. China's bedrock principle of non-interference – under which the South suffered during the war – is now welcomed in Juba as an attractive standard of engagement.[25]

Yang pledged assistance in economic and social development, beginning by gifting the construction of two secondary schools, a 500-bed hospital, a "friendship hall", and a national theatre.[26] He promised increased political, cultural, and educational exchanges and support for accession to international forums, and invited Kiir to make an official state visit to Beijing. Yang also identified the four areas which would frame China's initial economic engagement: energy, infrastructure, telecommunications, and agriculture. He also reiterated the expectation that existing oil contracts would be maintained and indicated interest in expanding investment in the sector.

The Chinese government hoped Kiir would visit before the end of 2011, but it was not possible. The embassy in Juba reports that his visit – now slated for April 2012 – remains its top priority, and a series of additional cooperation agreements are likely to be signed at that time. South Sudan has also been invited to join several Chinese-sponsored forums, most notably the Forum on China-Africa Cooperation (FOCAC), which institutionalises various forms of cooperation and opens another door to Chinese trade and development finance. Juba will send representatives to FOCAC's fifth ministerial conference in Beijing (a tri-annual event) in the summer of 2012.

The Chinese ambassador is now assisted by three political officers, a commercial advisor and a handful of support personnel, and Beijing plans to gradually expand the staff to twelve by adding further education, cultural, and consular officers.[27] South Sudan plans to open an initial 35 embassies in 2012, with Beijing to be one of four in Asia.[28]

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[21] Recognition and support for accession to the UN were soon echoed by Beijing's foreign minister and its representative to the UN.

[22] Crisis Group interview, cabinet minister, Juba, November 2011.

[23] Crisis Group interviews, Juba, telephone interview, China-Africa expert, February 2012.

[24] For more, see, "Photo Exhibition of the Chinese Medical Team in South Sudan", Embassy of the People's Republic of China (www.china-embassy.org), 25 August 2011. In January 2012, a Chinese delegation signed an agreement in Juba to send another medical team.

[25] Daniel Large, "South Sudan and China", op. cit., p. 284. Crisis Group interviews, Juba, November 2011.

[26] The "gift" package, which included other forms of support, is reportedly worth $200 million RMB ($ 31.5 million). Crisis Group interviews, Chinese officials, Government of the Republic of South Sudan (GoRSS) officials, Juba, November 2011.

[27] Crisis Group interview, Chinese diplomat, Juba, November 2011. Beijing's first representative in Juba was Zhang Qing Yang; the post is currently held by Li Zhiguo, who arrived in November 2010.

[28] Crisis Group interviews, foreign ministry officials, Juba, November 2011, February 2012. Recent austerity measures may curtail this number however, as well as limit the number of staff at each embassy. Salva Kiir issued a 7 March 2012 decree naming 78 ambassadors at varying grades, though they have not yet been assigned to embassies. Their deployment will report-

The Beijing embassy will be a high-profile post, and there is considerable speculation over who will be appointed ambassador. Chinese businesspeople hope an enhanced South Sudanese diplomatic presence in Beijing will facilitate greater and more efficient flow of nationals to Juba.[29]

China has been an important supporter – in political and material terms – for UN peacekeeping in Sudan since the early 2000s.[30] It backed the revamped mandate of the UN Mission in South Sudan (UNMISS) in 2011 and has buttressed its presence in the new country through continued troop contributions. Headquartered in Wau, Western Bahr al Ghazal state, its 350 peacekeepers are primarily an engineering contingent, and are now accompanied by combat troops per new integrated force protection arrangements.[31] In addition to engineering, construction, and maintenance of national infrastructure and UN assets, its personnel also operate a Level II UN hospital and staff force headquarters and mission support units. Commitment levels are expected to be maintained. Historically, China has invested diplomatically wherever it has stationed peacekeepers, and their presence on the ground in South Sudan may similarly bind Beijing to the practical and political success of UNMISS.

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edly be the responsibility of Foreign Minister Nhial Deng Nhial.

[29] Crisis Group interview, Chinese business owner, Juba, November 2011.

[30] China initially shielded Khartoum from international pressure over the conflict in Darfur in the mid-2000s, including by supporting the requirement for Sudanese consent to a peacekeeping mission that enabled Khartoum to thwart and delay deployment. But by mid-2007, China helped secure the government's consent to a three-phase deployment of a UN-AU peacekeeping operation (UNAMID). For a detailed review of China's role in UN peacekeeping in Sudan, see Crisis Group Asia Report N°166, *China's Growing Role in UN Peacekeeping*, 17 April 2009.

[31] Such force protection units were previously requested by China with regard to its participation in UNAMID, ibid. It played a role in negotiating the inclusion of such units in the mandate.

Bilateral Exchanges Between Beijing and Juba Pre-Independence

- September 2010: A South Sudanese delegation of ministers and state governors visits China as part of an agricultural and infrastructure study tour, engaging counterparts from the commerce and agriculture ministries. Given Chinese fears about the effects of secession on stability, the delegation also delivers a direct political message: the best way for Beijing to ensure its interests are protected is to develop strong relations with Juba, first and foremost by supporting the referendum on self-determination and recognising its outcome.[32]

- September 2010: Governor Taban Deng of Unity State – one of two oil-producing states – is invited to China to discuss the oil sector and advance relations. The visit demonstrates China's outreach beyond the national level, particularly to states and counties that host major Chinese investments, and follows on a history of corporate engagement with local representatives and commanders in areas of interest.

- October 2010: Du Yanling, director-general of the Communist Party's international department, leads the first party delegation to Juba, pledges enhanced engagement in energy, infrastructure, agriculture and services, and expresses concern over the security of oil investments. SPLM leadership provides assurances and requests help in pressuring Khartoum to honour the referendum and avoid a return to war.

- October 2010: Speaker of South Sudan's assembly, James Wani Igga, leads a delegation to China at a time when the exercise of South Sudan's referendum remains in doubt. Government officials – including Igga – had asserted the South would conduct the vote on its own should Khartoum not cooperate. His visit also includes talks with two Chinese construction firms, Zhong Hao Overseas, and INTECH Building.

- February 2011: Vice Foreign Minister Zhang Zhijun visits Juba, accompanied by a senior CNPC executive. He also seeks assurance from Juba on the security of oil investments and lays foundation for establishment of official diplomatic relations.

- March 2011: Finance Minister David Deng visits Beijing to invite President Hu Jintao to independence celebrations. Deng discusses improving payment and financial arrangements in light of complaints by Chinese companies and also seeks an emergency reserve loan to safeguard against a North-South oil standoff, but to no avail.[33]

- March 2011: Du Yanling returns to Juba to continue party-to-party consultations with the SPLM and invites SPLM leadership to visit Beijing.

- May 2011: Chang Xiao Dong, director-general for West Asia and North Africa in the foreign ministry, visits Juba to advance preparations for the establishment of diplomatic relations in July.

[32] Crisis Group interview, senior SPLM member of delegation, Juba, October 2010.
[33] Crisis Group interviews, finance ministry officials and economic adviser, Juba, November 2011.

Bilateral Exchanges Between Beijing and Juba Post-Independence:

- July 2011: President Hu Jintao dispatches Jiang Wei Xin, housing and infrastructure minister, to represent China at independence day celebrations in Juba and establish diplomatic relations. A senior official with close ties to the president, Jiang frequently represents him at official state ceremonies. Some South Sudanese see the choice of representative as a signal of Beijing's interest in the new country's infrastructure development.[34]

- August 2011: Foreign Minister Yang Jiechi visits Juba, outlining his government's positions with President Kiir and then-Foreign Minister Deng Alor. Chinese diplomats eagerly note that the foreign minister was the first of the five permanent members of the UN Security Council to undertake an official visit to the newly independent republic.[35]

- October 2011: SPLM Secretary-General Pagan Amum meets Communist Party (CPC) standing committee member Li Changchun in Beijing to discuss government and political party cooperation, as well as the security of Chinese investments.[36] He is welcomed by party leaders in Shanghai and Hunan province and observes agricultural engineering projects and emerging technology. The parties sign a memorandum of understanding, and a second SPLM delegation visits in November to learn about CPC operations.

- November 2011: Chinese Vice Minister of Commerce Jiang Yaoping leads a trade delegation to Juba, accompanied by a host of trade officials and more than 40 senior business executives. The delegation includes representatives from China's two premier policy banks and other financial institutions, as well as power, engineering, telecommunications, and construction firms. The minister signs a bilateral framework on trade and technical cooperation and delivers a gift of anti-malarial medicines to the health ministry. South Sudanese officials impress on Jiang their desire that China flex its muscles in getting Khartoum to sign a deal on oil.

- December 2011: Chinese state-owned construction company Sinohydro invites Roads Minister Gier Chuang to China to showcase and discuss road construction.

- January 2012: Li Yuanchao, a senior member of the CPC's Politburo, visits President Kiir and SPLM Secretary-General Pagan Amum in Juba, pledging aid and discussing a resource-backed loan. In addition to a preliminary framework on economic cooperation, his delegation also signs bilateral agreements on oil, capacity-building in the petroleum sector, water and health (including the dispatch of medical teams to South Sudan).

- February 2012: Simon Kun, governor of the oil-producing state of Upper Nile, is invited to China, where he discusses road and housing construction proposals for his state with private and state-owned firms.

[34] Crisis Group interviews, Juba, November 2011.
[35] Crisis Group interviews, Chinese diplomats, Nairobi, Juba, November 2011. The other permanent of the Security Council are Russia, France, the UK and the U.S.
[36] Changchun is one of nine members of the CPC politburo's standing committee, China's most powerful decision-making body.

III. CHINA'S ATTRACTIVE ECONOMIC COOPERATION MODEL

China's model for economic cooperation is as attractive in Juba as it has proven elsewhere in Africa. Chinese engagement on the continent is often met by traditional (OECD) donor countries with scepticism and anxiety – concerns fuelled by the often secretive nature of the engagement and aid arrangements[37] and Beijing's limited engagement in donor coordination and other multilateral cooperation.[38] While China's record in Africa, and Sudan in particular, merits some caution, it also increasingly hints at great opportunity and mutual benefit for developing states.

Many South Sudanese leaders express a desire to consolidate their historical alignment with the West, and the U.S. in particular, by welcoming their investment. But the red-tape, conditionalities, pace, and risk-aversion often associated with Western partnerships appear no match for the efficiency, speed, value, and perceived "no-strings-attached" model offered by China. A state governor asserted that while the U.S. and other Western partners might build better quality infrastructure, "the Chinese are here and ready to build now … the Americans … they just want to talk about politics and democracy".[39]

Despite recent U.S. attempts to boost South Sudan's visibility as an investment destination, Juba is frustrated by the slow pace of Western commercial engagement.[40] It is widely held that commercial deals with the West are often complicated and slow, whereas "if you sign an agreement with China [to build something], the next morning they are already working".[41] This view stems from Juba's own early experiences working with Chinese companies, but also from the opportunity of the country's elite to see the fruits of China's engagement, rapid resource mobilisation and infrastructure development in neighbouring states.

Low profit margins and cheap labour mean China also has a comparative advantage, particularly in building infrastructure, and can offer developing states the most for their money, but the model is not just attractive because it is cost-effective or comes with fewer demands on governance or human rights. As a South Sudanese official opined, "the U.S. and our other [Western] friends regularly tell us with certainty what we need. The Chinese appear more open to talking and to hearing what we want".[42] The Chinese also assert that they have lessons learned from their own extremely rapid growth over the last three decades to share with South Sudan.

A. Aid Architecture and Outward Investment

At the centre of China's complex aid structure are three principal institutions: the ministry of commerce, the Exim Bank and the ministry of foreign affairs. Aid normally comes from the commerce ministry in the form of grants or interest-free loans, while preferential loans and export credits are issued by policy banks. It is usually delivered in the form of project implementation, the contracts for which are awarded primarily to Chinese state-owned companies.[43] The commerce ministry's foreign aid department has the most clout; while the foreign ministry's permanent presence abroad is important in shaping policy, it cannot compete with its weightier government counterpart. Often a point of contention, and frustration for the diplomatic corps, foreign ministry inputs are at best complementary to the commercial responsibilities and aid strategy authority exercised by commerce.[44]

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[37] Deborah Brautigam, *The Dragon's Gift: The real story of China in Africa* (Oxford, 2009), p. 2. Crisis Group interviews, Juba, Beijing, February 2012.

[38] Western donors in Juba report little or no Chinese participation in joint donor forums. Crisis Group interviews, Juba, November 2011. However, China has reached out to the UN Development Programme (UNDP) and other relevant UN agencies in Juba to avoid duplication. Crisis Group telephone interviews, February 2012.

[39] Crisis Group interview, South Sudan, February 2011.

[40] In December 2011, the U.S. invited potential investors to a "U.S.-South Sudan Engagement Conference". High-profile speakers, including Secretary of State Hillary Clinton, were well received; the conference, aimed at attracting investors, however, met with mixed reviews. Stability, a solid legal framework and adequate commercial protections are concerns for many foreign investors, but the legacy of the old Sudan is a deterrent. Despite its independence, the country still suffers from historical associations, such as terrorism, economic sanctions, divestment campaigns, etc. South Sudanese and U.S. officials have attempted to persuade American companies to invest, but despite the lifting of all legal hurdles, some companies remain deterred by the prospect of negative attention. Crisis Group interviews, Juba, November 2011, Washington DC, December 2011.

[41] Crisis Group interview, cabinet minister, Juba, November 2011.

[42] Crisis Group interview, foreign ministry official, Juba, November 2011. Crisis Group interviews, GoRSS economic officials, cabinet ministers, Juba, November 2011.

[43] Bidding processes for aid contracts happen in China. Aid contracts have helped facilitate the entry of state-owned firms into Africa. Crisis Group interview, government-affiliated think-tank, Beijing, February 2012.

[44] The foreign ministry's comparatively weak status at home and abroad is reflected in the CPC leadership structure. As China's international influence grows, the number of internal actors playing foreign policy roles has grown and authority has become increasingly fractured. All this dilutes the influence of the foreign ministry. Crisis Group interviews, scholars and foreign policy experts, Shanghai, Beijing, February 2012; china expert,

The Exim Bank is one of two Chinese "policy" banks involved in foreign lending that are backed and heavily influenced by the central government.[45] Exim enjoys international credit ratings equivalent to those of the government, allowing it to attract capital that it can lend at sub-market interest rates on flexible payment schedules.[46] Combining private business with development objectives, the bank's overseas activities are often oriented to advance Beijing's trade and foreign policy objectives. Its stated mandate is to facilitate the import and export of Chinese products and technology, assist Chinese companies with comparative advantages in offshore projects and outbound investment and promote Sino-foreign relationships and trade.[47] But Exim's orientation continues to evolve toward more commercially oriented objectives.[48]

Much like the West's aid, Beijing's is employed as an instrument of foreign policy, designed to benefit China, in economic and political terms, as much as its recipient. Foreign aid is complemented by a policy framework that encourages Chinese companies to "go out" (or "go global"),[49] offering subsidies and other incentives for outward investment and the export of Chinese goods, technology, and equipment.[50] Business in Africa is also supported by funding mechanisms, such as the China-Africa Development Fund, that aim to bolster Chinese corporate development, as much as local development.[51]

Despite much success abroad, often in high-risk and high-return environments, Beijing's shift to outward investment has not been all smooth sailing. The realities of going global have created new challenges for Beijing and deepened debates about the viability of its "non-interference" policy. The evacuation of 30,000 Chinese workers from embattled Libya in 2011 marked a turning point. While the success of the operation ultimately drew domestic praise, the crisis posed a serious test for the government and subsequently raised expectations as to its willingness and ability to protect its growing citizenry and interests abroad.[52]

When 29 Chinese workers were abducted in January 2012 amid fighting in Sudan's Southern Kordofan state, the story grabbed headlines in China, the government came under intense pressure to act and the lack of a strong foreign ministry was exposed. Such incidents will continue to fuel debate in China about its overall posture in fragile states and not least in the two Sudans, as long as North-South relations remain volatile.[53] Given greater opportunities for investment around the world, some companies have begun to exercise more caution in high-risk areas in recent years, though the wealth of opportunity in South Sudan means most appear undeterred by recent events.

B. Economic Package/Loans

China has developed a series of investment and aid instruments that provide an economic foundation for its bilateral partnerships in Africa. They target a partner's development priorities but are also designed to support Chinese businesses on the continent and manufacturers at home. In resource-rich states eager to develop such as South Sudan, resource-guaranteed infrastructure loans are often a primary vehicle for engagement. Generous lines of credit are a catalyst for infrastructure development and in turn help secure China's energy and natural resource needs. Despite some misperceptions in Juba, such "loans" do not involve a transfer of cash, but rather designation of a resource envelope with specific terms pursuant to which the recipient

New York, December 2011. For an in-depth review of China's aid structure and characteristics, see Deborah Brautigam, *The Dragon's Gift*, op. cit.

[45] The other policy bank involved in foreign lending is the China Development Bank.

[46] The bank accumulates capital by issuing bonds on the interbank market. Its directives "are not profit oriented and fiscal obligations can at best be defined as accomplishing a balanced portfolio". "China's policy banks", *Caijing Magazine* (www.caijing.com.cn), 9 September 2009. Crisis Group interview, Beijing, February 2012.

[47] "Company profiles of Chinese delegation for promotion of trade & investment cooperation", China Chamber of Commerce for Import and Export of Machinery and Electronic Products, November 2011.

[48] Crisis Group interviews, foreign aid experts, Beijing, February 2012.

[49] The "go out" ("go global") policy, launched in December 2000, signalled a shift from inward to outward investment promotion. See Crisis Group Report, *China's Thirst for Oil*, op. cit., pp. 10-13. Since then, it has increasingly featured in the government's economic development strategy. In addition to political and investment guidance abroad, backing from government financial institutions has included subsidies on pre-investment costs, interest rates, and insurance for personnel working abroad. Duncan Freeman, "China's outward investment: challenges and opportunities for the EU", Brussels Institute of Contemporary China Studies, policy paper, 2008.

[50] Crisis Group interviews, Chinese entrepreneurs and business managers, Juba, November 2011. For more on the mechanics of Chinese government support to oil company investments abroad, see Crisis Group Report, *China's Thirst for Oil*, op. cit.

[51] Administered by the China Development Bank, the fund underwrites Chinese equity investments in Africa while promoting government policy objectives. Crisis Group interview, China-Africa expert, Nairobi, December 2011. Domestic production and competition also force companies to look abroad for new markets. Crisis Group interviews, Juba, November 2011, Beijing, February 2012.

[52] Crisis Group interviews, Beijing, November 2011, February 2012.

[53] Crisis Group interviews, scholars, foreign policy experts, Shanghai, Beijing, February 2012.

can draw down by contracting Chinese companies.[54] Those awarded contracts often use Chinese equipment and raw materials and employ skilled Chinese labour. An expert referred to this model as "one win for Africa, and two for China".[55]

Chinese construction firms setting up operations in Juba report they prefer this kind of loan financing, and many are lobbying Beijing accordingly. In addition to opening the door to substantial Chinese commercial engagement, such an arrangement allows companies in effect to be paid by the Chinese government, thus ensuring greater certainty of compensation, and often means enterprises can manoeuvre for more favourable terms than otherwise might the case.[56] It also allows them to be remunerated in U.S. dollars or Chinese renminbi (RMB) as opposed to local currency, thus avoiding conversion headaches. Furthermore, Chinese companies often work with Beijing's policy banks – and host governments – in developing projects themselves, a practice that has drawn some criticism from those who see it as unduly influencing host government development priorities.[57]

In the last decade, Beijing made major plays with resource-guaranteed loans in Angola, the Democratic Republic of Congo (DRC), and Ghana, most often used for developing infrastructure. These were disbursed by China's Exim Bank and secured against a natural resource.[58] The Chinese expressed an intention to offer economic support to Juba over the course of 2011, and rumours of multi-billion dollar loans circulated.

There are mixed opinions among government elites as to whether a large Chinese loan is a good fit for South Sudan. Some economic officials argue the country must first use its own resources more wisely. They cite insufficient capacity to handle a large-scale package and worry about focusing cooperation too heavily on Beijing. They also argue that competition will suffer if credit is tied to Chinese contractors alone. They instead propose seeking loans from a wider variety of actors, for clearly defined projects with clearly defined terms.[59] Cautionary voices also worry about future debt burden if oil revenues – virtually the country's sole income – decline as currently projected.[60]

By contrast, supporters of a sizeable Chinese loan argue the government must spend now to develop the infrastructure necessary to open up other revenue sectors and diversify an oil-dependent economy. The use of oil as collateral has growing appeal in Juba. Prior to the oil production shutdown,[61] few cabinet officials were aware that the draft petroleum bill – intended to guide government policy in the sector – would explicitly prohibit "any borrowing against future petroleum revenues". [62] This clause aimed to force a particular fiscal policy, though recent developments prompted the cabinet to eliminate it during its review of the bill in February 2012.[63] Opinions about loan financing continue to evolve in both Juba and Beijing, as the fiscal realities of the shutdown set in.

Negotiations toward a possible Chinese economic cooperation package only began to take firmer shape in early 2012, during the visit of senior CPC figure Li Yuanchao.[64] In addition to the 200 million RMB ($31.5 million) aid grant previously pledged by the foreign minister for fiscal year 2011, Li announced a second tranche of 200 million RMB from the commerce ministry for 2012, all of which remains to be disbursed. A $200 million favourable interest rate loan from Exim Bank was also reportedly offered. The third type of economic cooperation, a large infrastruc-

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[54] Often contracts have their own specific financing terms, under the umbrella terms set forth for the loan as a whole. Crisis Group interview, Deborah Brautigam, Washington DC, January 2012.
[55] Crisis Group interview, China-Africa expert, Washington DC, January 2012.
[56] Chinese businesses regularly complain about delays and other problems regarding payment for services rendered to the government of South Sudan. Crisis Group interviews, Juba, November 2011.
[57] Crisis Group interviews, Beijing, February 2012.
[58] Though political circumstances and financial structuring were unique in each case, the Exim Bank disbursed three separate loans to Angola totalling at least $4.5 billion and secured by Angolan oil exports to China (actual figures are difficult to determine, and may be significantly higher). The DRC was offered $6 billion, secured against copper and cobalt exports, while Ghana has been negotiating over a combined $13 billion from the Exim Bank and the China Development Bank, much of it to be secured against oil. The China Development Bank has recently increased its exposure on the continent and can offer similar loans. Crisis Group email correspondence, China experts, January 2012. Crisis Group interviews, Beijing, February 2012.

[59] The cabinet adopted an October 2011 resolution to begin pursuing concessionary loans for roads, power, water, and other infrastructure that exceeded budget capacity. Crisis Group interviews, finance officials, Juba, November 2011.
[60] Oil revenue constitutes some 98 per cent of South Sudan's total budget "Sudan: Country economic brief – February 2011", World Bank, February 2011, p. 2.
[61] The events leading up to the shutdown are addressed in Section VI below.
[62] The draft Petroleum Revenue Management Act (2011) states: "In order to preserve revenue streams from petroleum and ensure the object of this Act, there shall not be any borrowing against future petroleum revenues", Article 26 (2).
[63] Crisis Group interviews, Juba, February 2012.
[64] Leadership changes will take place in China during the CPC's eighteenth party congress in the fall of 2012, and it is widely believed that Yuanchao will be promoted to one of the party's top positions.

ture loan potentially guaranteed against future oil reserves, was also discussed, and a memorandum of understanding was signed that expressed Exim's readiness to facilitate such a loan.[65] A team of senior South Sudanese officials proposed eleven transformative infrastructure projects for such financing, which the Chinese delegation reportedly welcomed in principle.[66] These included construction of power facilities, national roads, national hospitals and universities. The parties agreed to establish a joint technical committee to review a possible loan package and calculate a price tag.

Views in Beijing about a loan package continue to evolve following this visit, however, as do priorities in Juba in the wake of the oil shutdown. Some Chinese officials remain concerned about a country still new to them and the caution demonstrated by other foreign investors. While open to additional projects, Exim Bank is not necessarily in a hurry to be out front in South Sudan or to invest as heavily as it has elsewhere in Africa. It has plenty of commercially attractive work to finance elsewhere and is naturally more conservative, as it bears fiscal responsibility for the loan. The foreign ministry – eager to cement political relations – is more keen for a sizeable loan package, and the commerce ministry, positioned as it is to promote Chinese business activity abroad, may also be in favour, as it would open the door for Chinese businesses, many of which are actively lobbying for loan financing.[67]

An economic cooperation package is likely to be announced during Salva Kiir's visit, as African presidents rarely leave Beijing empty-handed.[68] But how much, from where, and over what time period remain open questions, the answers to which will depend on a range of economic and political calculations. Chinese officials note that the shutdown of the oil sector and the continuing export crisis, if unresolved, could negatively affect the size of the total package.[69]

C. Economic Planning and Harnessing Foreign Investment

The kind of economic partnerships Juba forges will influence the character and stability of the state that emerges as well as its foreign policy, thus shaping its relationships and position in the region and beyond. Thus far, there appears to have been little strategic thinking as it relates to economic development and foreign investment partnerships. These must be considered with regard to all interested investors, but the rapidly-growing presence and signals from Chinese companies put Beijing at the forefront of the discussion.

A cabinet official expressed concern about insufficient strategic planning in the economic sector: "The Chinese are here attempting to carve out a role, and they are very proactive, but we the people of South Sudan have not yet defined a role for them".[70] A second senior political figure argued that in the absence of sufficient mapping and prioritisation of investments, China – and other eager foreign investors – will continue to drive the agenda.[71] Another influx of international investment may also distort the local economy and inflate prices. Juba should harness the new foreign interest so as to deliver on its development priorities, ensure cost efficiency through competitive bidding and demand quality delivery.

A strong legal framework, fair contracts and standards enforcement, transparency and oversight mechanisms – most notably in controlling expenditure – are critical. Considering both the fledgling state of its institutions and the fervour with which South Sudanese are seeking to put foreign money to work in developing the new nation, one official worried: "If we don't be careful, we could be looted in broad daylight".[72] Investment Promotion and Financial Management and Accountability acts have been adopted, but nine months on from independence, legislation regulating land, petroleum, petroleum revenue management, auditing, procurement and other critical areas is still in draft form. Adopting the relevant legislation is, however, only half the battle; enforcement will determine whether the laws ensure investor confidence and provide the new nation any protection. Juba has also begun to promote tax exemptions and other investment incentives,

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[65] A South Sudanese official involved reported that the Chinese "opened the conversation" by expressing readiness to loan $1 billion and indicated a willingness to further expand a loan package. Crisis Group interviews, senior SPLM officials, Addis Ababa, January 2012; Juba, February 2012; Beijing, February 2012.
[66] The team included SPLM Secretary-General Pagan Amum, Finance Minister Kosti Manibe, Cabinet Affairs Minister Deng Alor, Investment Minister Garang Diing, Roads Minister Gier Chuang and Electricity Minister Paul Mayom.
[67] Crisis Group interviews, Beijing, Juba, February 2012.
[68] South Sudan's foreign minister will lead an advance team to Beijing, presumably to secure agreement on the size and kind of cooperation to be announced. Crisis Group interviews, foreign ministry officials, Juba, February 2012.
[69] Crisis Group interviews, Beijing, February 2012.
[70] In addition to those projects already proposed, a foreign ministry official said committees have been formed that convene energy, finance, roads and housing officials to consider projects for proposed Chinese financing, but the status of their work remains unclear. Crisis Group interview, Juba, November 2011.
[71] Crisis Group interview, Juba, November 2011.
[72] Crisis Group interview, foreign ministry official, Juba, November 2011.

particularly for strategic and transformative investments.[73] However, resolving the oil crisis, and stabilising the new and fluctuating currency will also be necessary to attract and protect investment.

A business registry has been established to help ensure tax and other legal compliance, and more than 12,000 businesses have been established, which includes a considerable surge after July 2011. Because the process to establish a foreign enterprise is far lengthier and requires host government documentation, most foreign companies instead register as a local business in a matter of days. Businesses are required to file an annual activities report along with tax documentation, though the government has yet to strictly enforce compliance with commercial tax requirements.[74]

Corruption remains a serious concern. A significant shift to Chinese business and financing worries some – most notably Western donors – who would prefer to see capacity, accountability, and governance improve first, thus creating an environment in which business can flourish.[75] Sceptics fear the principle of non-interference, the economic model on offer, and the influx of private capital could undermine attempts to bolster such an environment. Corruption is often part of doing business in China, prompting worries that dubious practices will find fertile ground in the South, where millions of dollars of government revenue have already gone missing. A senior official complained that some Chinese companies are courting some ministers in attempts to land deals. His colleagues, he argued, "are not yet getting it … all contracts must go through the ministry of finance. This business of the last six years cannot continue".[76]

While the Chinese government often helps national firms enter markets and win contracts, it has far less capacity to regulate those companies' practices overseas than is commonly perceived. In response to appeals from international competitors on corruption, the Chinese claim insufficient capacity and legal frameworks to control the problem at home, much less abroad.[77] State-owned companies are sometimes subjected to a degree of oversight, and international criticism has prompted the government to pay greater attention to corporate social responsibility. Private companies, however, have been characterised as "outlaws".[78] Better business practices and government regulation must begin at home if they are to improve abroad.

While private businessmen are making in-roads at select ministries, official policy engagement with China remains concentrated among, and driven by, a handful of Juba's elite party and government officials. Capacity remains a shortcoming at many ministries where China's engagement will be relevant: foreign affairs, investment, agriculture, roads and bridges, electricity, water and irrigation, and petroleum and mining. New civil servants were appointed to many ministries in late 2011; some are still becoming familiar with their portfolios or are unaware of their ministry's prior engagement with China.[79] Investment prioritisation and policy planning remain limited at the national, and even more so at the state level.

When considering Chinese investment, South Sudanese often raise concerns about quality. This is due in large part to popular awareness of sub-standard rates of oil recovery associated with Chinese-led oil consortiums.[80] But in a place where development has been long-deferred and expectations are high, the demand for immediate investment and results largely outweighs such concerns. The challenge will be to ensure quality control with limited monitoring and evaluation capacity. Officials report that they intend, where possible, to couple infrastructure contractors with Western advisers and project managers, as there is a strong belief that quality standards are higher and technology more advanced in the West.[81] When considering low-cost bids, those who have done business with Chinese companies know that Chinese quality standards are often a function of "you get what you pay for", and that higher quality goods and standards are deliverable, but at a higher price.[82]

D. Competition Between China and the West?

South Sudan is open for business, and there is public and private interest from East, West and everywhere in between. Given both historical links to the U.S. and other Western nations, and the new interest from Beijing, a South Sudanese politician opined, "there will be a struggle for con-

[73] In 2009, Juba authorised duty exemptions (eg, on agricultural equipment) and tax incentives for what have been categorised as strategic and transformative investments, though their use has not been consistent. Investment Protection Act, 2009.
[74] Crisis Group interview, business registry official, Juba, November 2011.
[75] Crisis Group interviews, Juba, November 2011, New York, December 2011, Washington DC, January 2012.
[76] Crisis Group interview, December 2012.
[77] Crisis Group interviews, November 2011; Beijing, February 2012.
[78] Other complaints raised by African and international companies include poor labour standards, local employment practices and the effects on local economies prompted by an influx of Chinese goods. Crisis Group interviews, Beijing, February 2012.
[79] Crisis Group interviews, civil servants, Juba, November 2011.
[80] Crisis Group interviews, Juba, Bentiu, Malakal, 2009-2011.
[81] Crisis Group interviews, Juba, November 2011; Addis Ababa, January 2012.
[82] Crisis Group interviews, Juba, November 2011; Beijing, Shanghai, February 2012.

trol here between China and the West".[83] The geostrategic value of South Sudan should not be over-stated, however, and many in Beijing and Western capitals argue there is room enough for all. But the undertones of economic and political competition that sometimes colour engagement in Africa are perceptible in South Sudan.[84]

Despite the contrasting approaches of development partners and some varying geopolitical preferences among the country's elite, Juba is generally keen to welcome all.[85] As such, it has an opportunity to leverage the options now in front of it, using competitive (and less conditional) offers of Chinese investment to secure more favourable engagement with Western states and firms. Washington's December 2011 decision to free South Sudan's petroleum industry from sanctions may eventually draw Western companies back to the oil sector, where China now dominates.[86]

While China enjoyed an advantageous economic relationship with Khartoum, its companies will face more competition in the South. Chinese officials are confident of their comparative advantages,[87] but while a broader field will not discourage Chinese investors, it may demand finer calibration of their relations with the government, as they are no longer the sole financial lifeline.

Chinese suspicions about U.S. policy motives are not insignificant; officials cite a pro-South Sudan bias in Washington, and some wonder whether American support for the referendum and independence was not only a step toward a goal of regime change in Khartoum, but possibly also meant to counter China's growing economic prowess in Sudan and the region.[88] This is indicative of an anxiety about U.S. foreign policy that extends well beyond the two Sudans.

Chinese officials have made clear to American officials – both publicly and privately – their concerns over U.S. motivations for NATO's March 2011 intervention in Libya, as well as for the October 2011 deployment of 100 U.S. Special Forces to central Africa in pursuit of the Lord's Resistance Army and its leader, Joseph Kony.[89] In both instances, they have wondered whether the move was somehow aimed at weakening China. Chinese observers note such distrust is driven in part by aversion to universalist tendencies and concerns about the perceived export of Western-style democracy.[90]

While there is considerable mirrored concern and misunderstanding about China in the West, better-informed actors seek to promote cooperation and frame China as a partner, not an adversary, in Africa. Many governments and development agencies are beginning to explore opportunities for development cooperation with Beijing.

U.S. Assistant Secretary of State for Africa Johnnie Carson had lengthy discussions in Beijing in November 2011 as part of the "U.S.-China Sub-Dialogue on Africa", a forum established in 2005 as part of a broader U.S. effort to engage an emerging China in a more constructive manner

[83] Crisis Group interview, senior politician, Juba, November 2011.
[84] A U.S. official explained that when Juba needs help, "they still call on us first; but we could exact more pressure when we were in a position to help deliver independence". Now, "the China appeal makes it harder for us to apply pressure bilaterally". Crisis Group interviews, diplomats, foreign policy experts, aid officials, businesspeople, government officials, Juba, Nairobi, November 2011, Washington DC, January 2012, Beijing, February 2012.
[85] Some in the SPLM's top tier exhibit a stronger orientation to the West and persistent hesitations about China, though most are open to whoever will help. Some Chinese argue that if Beijing is to root its strategic engagement in South Sudan beyond mutual economic gain, it must enhance other forms of cooperation, including those already exercised by established partners such as the U.S. A Chinese investor with experience in the region explained that Beijing must continue to diversify its modes of engagement: "Look at the size, location, and role of the American embassy; look at how many Sudanese students are educated in the U.S., look how many ties there are to established diaspora there". Crisis Group interviews, Juba, August, November 2011.
[86] This will depend, in part, on greater stability in the oil sector and the relationship with Khartoum. Following recognition of independence, the U.S. government expressed a view that "South Sudan was born a sanction-free country", though in practice that was not immediately the case. Given continuing economic interdependence between the two countries – most notably in the oil sector – some sections of the regulations still prohibited business in the South's petroleum industry, insofar as it benefited the petroleum industry in the North. On 8 December 2011, an order from the treasury department signalled a re-interpretation of the existing sanctions regime, which prohibits transactions in Sudan's petroleum and petrochemical industries. The new licenses allow transactions in South Sudan's industry and the transhipment of goods through Sudan (to or from South Sudan), insofar as they afford "maximum benefit to the South and minimum benefit to the North". In March 2012, President Obama also declared South Sudan's eligible for a preferential trade program, the Generalised System of Preferences; eligibility for the African Growth and Opportunity Act is pending.
[87] Crisis Group interviews, Nairobi, Juba, November 2011, Beijing, February 2012.
[88] Crisis Group interviews, officials and representatives of policy think-thanks, Beijing, Nairobi, Juba, November 2011.
[89] Crisis Group interviews, Beijing, November 2011; U.S. State Department official, Washington DC, January 2012. Chinese officials lamented that they first learned of the U.S. deployment through the media rather than directly from U.S. diplomats. The establishment of the U.S. Defense Department's Africa Command (AFRICOM) in 2008 raised fears about the impact of a greater military footprint on Chinese investments and relationships on the continent, though such concerns have since faded.
[90] Crisis Group interviews, Juba, Beijing, Shanghai, November 2011, February 2012.

on African issues. Carson pressed the Chinese to be responsible actors on the continent by refraining from corruption and by following fair business practices with regard to both national hosts and international competitors. He emphasised the mutual interest in stability in the two Sudans and the hope China would employ its strengths to complement U.S. efforts to that end.[91] Chinese Vice President Xi Jinping reiterated this sentiment during his high-profile visit to Washington in February 2012. Xi sought to identify issues for broader policy engagement and specifically cited the Sudans to President Obama.[92] Likewise, Western officials have welcomed the balancing of China's position that has accompanied its shifting relations with Khartoum and Juba, noting more common ground on policy in forums such as the UN Security Council.

There is, however, no shortage of criticism of China's engagement model, interests and intent on the continent, or of anxiety about the effects on both U.S. commercial interests and efforts to shape liberal democratic states.[93]

Defence cooperation is a regular component of China's diplomatic relations, and its military leaders have established some kind of relationship with each African state with which it has official ties.[94] In some cases – Sudan is one – cooperation is extensive and involves a considerable arms trade. In others, it is limited to occasional military-to-military exchanges. Defence cooperation does not figure prominently in China's courting of South Sudan at present, though Chinese officials signal that it may in the future.

Given South Sudan's existing relationship with the U.S. military, the shape of any potential defence cooperation with China or others may depend in part on how the relationship with Washington develops. The U.S. military's Africa Command is completing belated assessments of the Sudan Peoples' Liberation Army (SPLA), which will then be submitted for an inter-governmental review process to determine the precise U.S. support to the security sector. Washington's current financial state, as well as SPLA conduct, will be among the factors dictating the content of that support package.[95]

In January 2012, President Obama declared South Sudan eligible to receive defence articles and services.[96] The declaration was largely pro-forma, necessary to facilitate enhanced security sector support. It allows for arms sales, but there is no intention at present to provide South Sudan with lethal weapons.[97] Even if the SPLA otherwise intends to procure sophisticated weapons, U.S. officials see such provision as too provocative in the still tense North-South environment. Not least given persistent tensions with Sudan, the SPLA maintains that "we must arm ourselves, as the international community will not come to our rescue",[98] U.S. defence department officials report they are unlikely to help facilitate acquisitions and have no interest in delivering on unrealistic SPLA wish lists, given "they are not capable of operating or maintaining" much of what they have requested.[99]

The SPLA will undoubtedly look elsewhere to buy what it wants, including to China and others who may attach fewer conditions to arms transfers.[100] Southern forces have traditionally fielded Eastern bloc weapons, so purchases

[91] Crisis Group interviews, U.S. officials, Washington DC, New York, January 2012.
[92] Foreign Minister Yang Jiechi also raised Sudan and South Sudan during his parallel meeting with U.S. Secretary of State Hillary Clinton. Crisis Group email correspondence, telephone interviews, diplomats, February and March 2012.
[93] Fair or not, the view often perpetuated in Washington and European capitals is that China is in Africa solely for its own interests, while the West is pursuing a broader and more principled agenda. A confidential U.S. embassy cable from 2010 illustrates some of the more ardent expressions of U.S. reservations about China. In addition to lamenting Beijing's partnerships with authoritarian strongmen on the continent, Assistant Secretary Carson cautioned his African counterparts: "China is a very aggressive and pernicious economic competitor with no morals. China is not in Africa for altruistic reasons. China is in Africa for China primarily …. The United States will continue to push democracy and capitalism while Chinese authoritarian capitalism is politically challenging". "US monitors China and its expanding role in Africa", U.S. embassy Malabo, 23 February 2010, as made public by WikiLeaks.
[94] China has diplomatic relations with 50 of the 54 states in Africa. Crisis Group interviews, Beijing, February 2012, Washington DC, January 2012.
[95] Assessments of SPLA conduct include respect for human rights, as well as Washington's discontent over continued support for Sudanese armed opposition groups that had been aligned with Juba before independence. Support is likely to begin by strengthening capacity within the defence ministry, followed by training in command-and-control, communications, logistics and the like. Crisis Group interviews, U.S. defense department officials, Washington DC, January 2012, March 2012.
[96] "Presidential Memorandum – Presidential Determination on the Eligibility of South Sudan to Receive Defense Articles and Defense Services", Office of the White House Press Secretary, 6 January 2012.
[97] Crisis Group interviews, U.S. defense department official, state department official, Washington DC, January 2012.
[98] Crisis Group interview, SPLA general, Addis Ababa, January 2012.
[99] Crisis Group interview, Washington DC, January 2012.
[100] Russia and Israel are reportedly among the other nations that have approached the SPLA regarding weapons acquisitions and military cooperation. Crisis Group interviews, Western defence official, January 2012, Nairobi, March 2012. Though Chinese companies authorised to export arms are "state-owned and staffed with military and politically connected appointees, they are profit-making enterprises with commercial objectives". "China's growing role in African peace and Security", Saferworld, January 2011, p. 49.

from China would ensure consistency of supply.[101] Thus far, however, China has not initiated substantive security discussions with the government or the army, other than to signal a general willingness to cooperate.[102]

Defence also figures in Southern desires for China to reorient its relationship with Khartoum. As North-South tensions continued to escalate in November 2011, the vice chairman of China's Central Military Commission pledged an expansion of military-to-military cooperation during a visit by Khartoum's defence minister.[103] Though a standard interaction, the visit also signalled Beijing's intention to maintain strong relations with Sudan. But the timing caused some in the South to complain: "Chinese companies want a stable investment environment, but they [China] keep selling arms that destabilise the borders and drive conflicts [in Southern Kordofan, Blue Nile, Darfur, and Abyei]".[104]

101 Most Chinese infantry weapons, including AK assault rifles, are based on former Warsaw Pact standards and use the same ammunition.
102 Crisis Group interview, SPLA general, Addis Ababa, January 2012.
103 "China pledges to boost military cooperation with Sudan", *Sudan Tribune*, November 2011.
104 Crisis Group interview, senior cabinet official, Juba, November 2011.

IV. NON-OIL SECTOR INVESTMENT

Following the signing of the CPA in 2005, a handful of Chinese investors braved entry into an unknown market, seeking to turn a profit in an untapped but high-risk environment. Independence has again prompted new commercial interest and turned the handful into a flood of competing would-be investors. The number of Chinese nationals – most of them businesspeople – in Juba has skyrocketed. Many work for companies that already have a considerable footprint on the continent; others are straight from China. Much of the buzz is still preliminary, as, for the most part, major contracts are yet to be landed. Executives and delegations are instead discussing projects and pitching proposals, making introductions, glad-handing ministry officials and launching feasibility studies. As huge contracts are up for grabs, there is also considerable secrecy and competition between major Chinese firms.

Many are registering their businesses, most often as local companies. The business registry reports that Chinese companies constitute the largest number of non-African foreign businesses registered locally, as well as the largest number of all businesses registered as foreign companies.[105]

Business is happening at all levels; large private corporations and state-owned enterprises are active – the latter of which are today far less influenced by the state than is commonly perceived in Juba.[106] But service industry and import/export entrepreneurs have arrived in greater numbers as well, as have small-scale merchants selling cheap consumer goods. Chinese businesspeople often promote the view that China is interested in long-term investment in South Sudan, though observers say this is little more than good public relations.[107] Most operators import many materials they need from China, or if necessary from elsewhere in the region. Many companies – particularly those already established in the region – employ labourers primarily from neighbouring Kenya and Uganda; where local labour is used, complaints sometime arise over lack of skills and work ethic.[108]

105 Crisis Group interview, business registry official, Juba, November 2011.
106 As China's economic transformation continued in the 1990s, the structure of most state-owned enterprises likewise evolved. Today the central government remains a majority shareholder but is removed from day-to-day operations and management. Managers in Juba regularly note that the government has little or no influence on company direction, investments, or operations.
107 Crisis Group interviews, Juba, November 2011; Beijing, Shanghai, February 2012.
108 Crisis group interviews, Chinese business representatives, Juba, November 2011.

Despite the spike in Chinese commercial interest, many with experience in South Sudan have had their high expectations tempered in recent years; complaints include lack of basic materials, as well as high operating and transport costs (and thus smaller profit margins), delays and other headaches in securing payment, and sometimes unwarranted – or at least misunderstood – government fees. One manager complained operating costs were four times higher than for his other projects in East Africa.[109] Not unlike other foreign nationals, Chinese also complain of political/social instability, difficult living conditions, disease, and occasional harassment by security personnel.[110]

A. Infrastructure

Outside of oil, infrastructure is the dominant Chinese interest and will likely be the primary area of economic cooperation, particularly if facilitated by a sizeable loan. The world's newest and least developed nation has a long list of needs, including roads, bridges, power plants and electricity grids, hospitals and municipal buildings, water treatment facilities, dams and irrigation systems, and new oil infrastructure (potentially including refineries and an export pipeline).[111] The infrastructure deficit has drawn more construction firms to Juba than any other kind. In addition to subsidised financing, the low cost of Chinese labour and access to imported raw materials, Chinese often tout their work ethic, experience in the region, and efficiency as bases for their comparative advantage.

The prospect of a new South Sudanese capital at Ramciel,[112] as endorsed by the cabinet in September 2011, has also tempted major Chinese construction companies. Though the capital project is a long way from becoming a reality, and funds are now undoubtedly jeopardised by the shutdown of the oil sector, the prospect of multi-year, multi-billion dollar contracts generated considerable competition in 2011. Bids for mapping and surveying of the proposed capital were opened in December, and Sinohydro and Pan-China Construction were two of the six firms short-listed.[113] Companies have also expressed interest in the next phase, which will involve a design bid and has already generated controversy after it was falsely reported in October 2011 that Pan China was awarded the contract.[114]

There is no shortage of rumours as to what projects Chinese companies are pursuing. A handful of preliminary agreements have been penned, but none are certain contracts.[115] For the most part, major deals are yet to be signed, in part because of Juba's new financial constraints and in part because companies are awaiting, and lobbying hard for, finalisation of an infrastructure loan from Beijing.

Roads are among China's most visible contributions in Africa and will be also in South Sudan. Juba ranks roads among its top priorities, as even the few that are normally reliable in the vast country are often impassable during the rainy season. An expanded network would facilitate service delivery, security, and trade, including access to markets, links to new oil exploration areas and the opening-up of non-oil revenue sectors such as agriculture.

Juba announced its ten-year road development plan in January 2012, totalling more than 12,000km at a projected cost of over $6 billion.[116] The ten-state plan aims to connect state capitals as well to link each capital to Juba. First-tier priority routes include two national roads (the N1 and N2) and three additional junctions. Second-tier priorities include two more national roads and a series of feeder routes.[117]

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[109] Crisis Group interviews, Juba, November 2011.

[110] Crisis Group interviews, managers from large private and state-owned companies as well as small-business owners, Juba, November 2011.

[111] Needs and high post-independence expectations have prompted ambitious plans in many sectors, which fuel the demand for fast and cost-effective construction. For example, there is today very limited access to electricity, and generators still constitute a considerable portion of power production, including in the capital city. An ambitious government plan aims to electrify more than 70 per cent of the country by 2020.

[112] Ramciel is in Lakes state, near the junction of Jonglei and Central Equatoria States, and thus at the centre of the South's three historical provinces, Upper Nile, Equatoria and Bahr al Ghazal.

[113] GoRSS press release, 6 December 2011.

[114] The claim was rejected as premature and false by both Pan China and the relevant government authorities, and corrections were published. Crisis Group telephone interview, senior official, housing and physical planning ministry, February 2012. Ater Garang Arieth, "Minister dismisses contract award to Pan-China Construction", *The Citizen*, 2 November 2011.

[115] A preliminary agreement was signed in February with state-owned infrastructure giant Gezhouba for construction of a hydropower station. The project is to be completed over seven years at a cost of $1.4 billion. The company will seek financing from the Bank of China. "China Gezhouba secures US$1.4 bln-contract in South Sudan", *China Knowledge* (www.chinaknowledge.com), 1 February 2012. Chinese Machinery Engineering Corporation has reportedly made headway toward a bid for a cement factory in Eastern Equatoria, but this is likewise yet to be finalised. Crisis Group interviews, cabinet officials, Juba, November 2011.

[116] For major roads, the roads ministry estimates costs of $1.2-$1.8 million per km. These figures are based in part on road construction budgets implemented by USAID, though many areas will cost more than current U.S. projects, depending on the terrain. Crisis Group interview, roads ministry official, Juba, November 2011.

[117] See Appendix B for a map illustrating the road development plan. The proposed "N1" runs South-North linking to Uganda

The ambitious plan, however, is backed by almost no budgetary allocation. The council of ministers in December approved a plan to seek $679 million in loans to finance road infrastructure in 2012 and $750 million for the following year – a pace that will have to continue for the next decade to achieve the goals identified.[118] In addition to likely credit from the International Monetary Fund (IMF), African Development Bank and others, China's Exim Bank is among the major financiers that have engaged the roads ministry directly, and it is capable of mobilising funds faster than most other creditors. Aside from contracts for a few sections of the N1 undertaken prior to independence, no major contracts have been signed as of March 2012.[119]

The largest and most visible road project undertaken so far is one funded by the U.S. Agency for International Development (USAID) linking Juba to Uganda via the border town of Nimule, the initial section of the N1. Nearly complete, it spans 192km and costs an average of $1.1 million per km.[120] However, the project experienced delays and additional costs, reportedly in part due to problems with several sub-contractors.[121] USAID will soon shift its focus to smaller feeder roads to complement its agricultural development strategy. Companies implementing road contracts prior to independence stopped due to political uncertainties or national budgetary revisions.[122]

Thus, the field for new contracts is wide open, and senior roads ministry officials report being overwhelmed by interested Chinese construction firms. A variety of other international firms have expressed interest, but the Chinese far outnumber other prospectors. Companies that have expressed interest or are undertaking feasibility studies include: China First Highway Engineering Company, China Railway No. 5 Engineering Group, China Harbour Engineering Group Ltd., China High-Speed, China Road and Bridge Corporation, CGC Overseas Construction Company Ltd., China State Construction Engineering Corporation Ltd. and Sinohydro Corporation.[123]

Chinese Companies Active in Infrastructure[124]

<u>Zhong Hao Overseas</u>, a Beijing headquartered private construction firm and one of China's largest international contractors, has been operating across South Sudan since 2006. It has built water supply and sanitation facilities (including more than 1,000 boreholes under UN agency contracts), government housing, a teaching hospital, roads, and a series of multi-purpose buildings. It operates in coordination with a regional hub in Uganda.[125]

<u>Sinohydro Corporation</u>, a major state-owned engineering and construction company based in Beijing, operates in a wide variety of infrastructure and engineering sectors, with a particular focus in hydropower. Active in Sudan for many years, Sinohydro is looking to expand in the South. Notable projects undertaken include a water plant in Western Equatoria, a 37km-city roads project in Malakal and a section of the N1 highway from Renk to Malakal – what will ultimately be a primary artery between Sudan and South Sudan.[126] Like many other large firms, Sinohydro is also interested in big-ticket road contracts and in securing a role in building the new capital at Ramciel.

B. TELECOMMUNICATIONS

Telecommunications is an area where Chinese engagement has been driven by companies rather than the state.[127] Mobile phone coverage remains extremely limited in rural areas, where most of the population resides, and mobile connectivity continues to experience significant problems even in Juba, as the government is yet to assume full control of the sector in the wake of partition. Five licensed mobile operators are active in South Sudan; most receive primary infrastructure, equipment, and operations support

and Sudan, via: Nimule-Juba-Bor-Malakal-Renk; the "N2" links to Kenya and runs mostly East-West, connecting Nadapal-Kapoeta-Torit-Juba-Mundiri-Rumbek-Tong-Wau-Kwajok-Aweil-Abyei. Priority junctions connect Mundiri to Yambio, Rumbek to Bentiu, and Wau to Aweil. Crisis Group interview, deputy roads minister, Juba, November 2011.

[118] "South Sudan seeks over $600 million from international banks", *Sudan Tribune*, 3 December 2011.

[119] Crisis Group interviews, senior roads ministry officials, Juba, February 2012.

[120] Cost calculations for this road include eight bridges and considerable de-mining activities, as well as management costs related to contract termination and re-bidding processes. Crisis Group email correspondence, USAID officials, February 2012.

[121] Sub-contractors included Kenyan, Turkish, Sudanese, and Indian contractors; the latter two of which were let go after significant problems, according to U.S. officials. Crisis Group interview, USAID official, January 2012.

[122] Crisis Group Report, *South Sudan: Compounding Instability in Unity State*, op. cit.

[123] Crisis Group interview, roads ministry officials, Juba, November 2011.

[124] The series of text boxes in the following pages highlight Chinese businesses active in South Sudan; they are not exhaustive but rather illustrative of the kind and diversity of growing Chinese investment in South Sudan.

[125] Crisis Group interview, Zhong Hao managers, Juba, November 2011.

[126] Crisis Group interviews, Sinohydro manager, deputy roads minister, Juba, November 2011. Sinohydro began the Renk-Malakal project in 2009 with partial funding from Khartoum, which cut that money off from the "unity" project in January 2011. Juba plans for Sinohydro to re-initiate work when financing is secured.

[127] The telecommunications ministry reports that it presented its fibre optic backbone vision to a delegation of Chinese government officials in 2008, but continued uncertainty over future stability and the referendum meant discussions went no further.

from two Chinese telecom giants: Huawei and Zhongxing (ZTE).

The telecommunications ministry is still formulating plans to expand mobile coverage and wants to extend broadband connectivity through a national fibre optic backbone network, which will require both public and private capital. Both Chinese companies have indicated interest in conducting feasibility studies and projects to expand connectivity, but their engagement has otherwise been exclusively with private operators, meaning the still emerging ministry is not fully abreast of their activities.

Officials argue telecommunications companies have enjoyed a holiday in South Sudan, as the government is yet to collect its own licensing fees or regulate the sector.[128] A draft bill aims to rectify that and complete the transfer of telecommunications administration from Khartoum. New roll-out plans were due from mobile operators in March 2012, and officials hope the bill will provide them the authority to demand better mobile coverage and inter-network connectivity and push operators to rural areas. Officials also argue the sector could generate considerable revenue and jobs and facilitate enhanced economic activity, so should be prioritised in step with other infrastructure development. Chinese telecom managers envision considerable opportunity for long-term business, as the government aspires to expand the system country-wide,[129] though profitability in rural expansion remains an unanswered question.

In 2010, Huawei applied for $120 million from Chinese policy banks to finance the extension of fibre optic cables from Kenya to the eastern portion of South Sudan; however, Khartoum's central bank declined to facilitate the transaction. As proposals began to materialise, Chinese commerce ministry officials encouraged telecommunications officials to instead orient business to ZTE, noting that its state ties would facilitate rapid government sponsorship and mobilisation. Major firms like ZTE, with close ties to the government, often work with China's policy banks to finance overseas projects that complement Beijing's strategic engagement on the continent.[130] Huawei also signed a memorandum of understanding with South Sudan's government to build, equip, and connect a National Information Centre, but finite government resources have put this project on hold.

Chinese Companies Active in Telecommunications

Huawei, China's largest provider of telecommunications equipment and services, has been working in South Sudan since 2004 and conducts operations in all ten states. The Guangdong-based multinational is among the world's mobile telecommunications giants and provides network infrastructure, equipment, and operational services to three of South Sudan's primary mobile phone operators: Zain, MTN and Gemtel. During the South's liberation struggle, Huawei engineers were active in SPLM-strongholds in Rumbek and Yei, offering equipment and services on a loan basis to help set-up Gemtel, the first mobile network used exclusively in the South.[131] The company's size, reputation, and government links mean it is one of the only private companies awarded contracts under Chinese aid (not loan) packages.

Zhongxing Telecommunication Equipment Corporation (ZTE) is a publicly-traded multinational with majority government share, second in size only to Huawei. It offers equipment, services, and software to more than 500 mobile network providers in 140 countries and is one of China's biggest manufacturers of mobile devices. Shenzen-based ZTE reported revenues of more than $10 billion in 2010.[132] It grew out of state-owned entities in 1985, retains close ties to key government ministries and was publicly listed in 1997.

C. Agriculture

Despite considerable arable land, South Sudan imports the vast majority of its food. Little land is cultivated for domestic consumption or commercial sale. Given declining projections for oil production, agriculture is widely viewed as the next centrepiece of South Sudan's economy, and the transition must happen fast. As elsewhere on the continent, Chinese officials often cite agriculture as a primary area for cooperation, but little government or private investment has materialised so far.

At present, Chinese plans in South Sudan appear limited to technical support and a handful of proposed "agricultural demonstration centres", in which experts would train local farmers to boost production on land granted by the government. Both have been staples of China's aid packages to Africa for decades. However, reviews of the demonstration centres are mixed; critics say they have not been able to translate their on-farm innovations into off-farm success in countries that do not have the networks, institutions, or resources to scale up.[133]

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[128] Crisis Group interviews, telecommunications ministry officials, Juba, February 2012.
[129] Huawei's operation in South Sudan falls under a regional headquarters in Egypt, one of three regional hubs in Africa. Crisis Group interview, Huawei executive, Juba, November 2011.
[130] Crisis Group interviews, Beijing, February 2012. Deborah Brautigam, *The Dragon's Gift*, op. cit., p. 116.
[131] Crisis Group interviews, cabinet minister, telecommunications official, Juba, November 2011, February 2012.
[132] "ZTE announces 2010 annual results", ZTE (www.zte.com.cn), 18 March 2010.
[133] Crisis Group interview, Beijing, February 2012.

Chinese officials report a vague possibility that in the future their companies could grow crops for export to China, where food consumption has increased on average 23 per cent every year for the last decade.[134] However, few Chinese development experts envision a need to grow food in Africa in the near term, and food is not presently being imported in any substantial quantity from the continent.[135] Furthermore, there appears to be some recognition in Beijing of the political sensitivities of exporting food from countries that struggle to feed themselves.[136]

Diplomats report that some companies have expressed interest and plan to send assessment teams, but such interest appears limited; as of late 2011, the new agriculture minister reported no contact with Chinese interlocutors of any kind.[137] Some experts argue that while agriculture is touted as a major Chinese interest in Africa, the reality does not often match the rhetoric. Agriculture often features in partnership arrangements with developing African states, and is encouraged by Beijing's ministries and banks, but large commercial projects rarely materialise.[138]

Experts note that while the government encourages investment, "word has gotten out" in the Chinese business community that agriculture in Africa is difficult and profit margins minimal.[139] Reservations about long-term investment sectors are compounded in South Sudan, where infrastructure is almost non-existent. Where the Chinese have demonstrated interest in large-scale projects in Africa, they, like the West, are most often not interested in growing food but in products such as biofuels, oil palm, sugar cane and the like. Where the Chinese are interested in growing food, the aim is to turn a profit in the domestic market.[140]

Given a series of questionable acquisitions by foreign investors in recent years, land grabbing has been identified as a considerable risk in South Sudan. China is often unfairly assumed to be a culprit in such activity, but land experts report no evidence of large Chinese acquisitions to date.[141]

In addition to planned demonstration centres, Beijing has also made offers to transfer technology and provide material support. In September 2010, then Ministers Awut Deng Acuil and Anne Itto led a delegation to China on an agricultural study tour.[142] The World Bank-supported delegation also included three state governors (Jonglei, Warrap, and Western Equatoria) and a series of state-level agriculture officials. It made stops in Beijing, Shanghai and Zhejiang and Hunan provinces, the latter the hub of Chinese agricultural research and activity.[143] Delegation members held discussions with the commerce and agriculture ministries and requested the supply of tractors other equipment and spare parts to be used at the state level for government-directed agricultural pilot projects. The Chinese agreed and invited the delegation to send back a team of technical experts to choose equipment and be trained on its operation and maintenance.[144] However, in large part due to a focus on the referendum and independence, South Sudan did not follow through. The initiative is yet to be picked up following a cabinet re-shuffle in August 2011, much to the frustration of the Chinese.[145]

D. Service Industry

Chinese entrepreneurs operate a wide range of enterprises, from hotels and restaurants to furniture stores and pri-

[134] Southern officials report that any such arrangement would only be possible if the government was a major partner. Crisis Group interviews, cabinet officials, Juba, November 2011. Simon Freemantle and Jeremy Stevens, "China's food security challenge: what role for Africa?", Standard Bank, 18 November 2011. Though stable, food security is a concern in China, which must feed more than 20 per cent of the world's population with roughly 7 per cent of the world's arable land. Annex 3: Agricultural policy and food security in China, in "Poverty alleviation and food security in Asia: lessons and challenges", Food and Agriculture Organisation (FAO) Regional Office for Asia and the Pacific, December 1998.
[135] Crisis Group interviews, Beijing, February 2012. In 2009, agricultural trade between China and Africa represented just 4 per cent of total trade. In terms of meeting China's food needs, "Africa, for now, does not feature prominently in Beijing's prospectus". Freemantle and Stevens, "China's food security challenge", op. cit.
[136] Crisis Group interviews, China-Africa expert, Washington DC, January 2012, foreign policy experts and academics, Beijing, Shanghai, February 2012.
[137] Crisis Group telephone interview, November 2011.
[138] Crisis Group interview, Deborah Brautigam, Washington DC, January 2012.
[139] Crisis Group interviews, economist and China expert, Washington DC, January 2012, Beijing, February 2012.
[140] Crisis Group interviews, Beijing, February 2012; Washington DC, January 2012.
[141] Crisis Group email correspondence, South Sudanese land expert, January 2012. A Chinese foreign policy expert described an at times active government policy of discouraging companies from purchasing land overseas given the political headaches associated with land-grabbing accusations. Crisis Group interview, Beijing, February 2012.
[142] Awut Deng was then labour and public service minister; Anne Itto was the agriculture minister.
[143] On exhibit were farming techniques, agricultural products and equipment, seed storage and soil management practices, and rice production with the famous Chinese scientist Yuan Long Ping, the "father" of hybrid super rice.
[144] Crisis Group interview, member of the delegation, Juba, November 2011.
[145] Crisis Group interview, Juba, November 2011.

vate clinics.[146] Chinese traders are selling construction materials, electronics and a wide range of cheap consumer goods, either directly or via local partners. Many hotels encompass a broad range of complementary businesses that together cater primarily to a Chinese commercial clientele, including restaurants, travel agencies, business centres, office space, transport and administrative services. Many small businesses that were operating in Khartoum have now opened outlets in Juba. Some acknowledge that competition will be greater in the South; one hotel owner was uncertain about the ability to compete in the long run, as "the West is rich".[147] Chinese businessman and labourers concentrate primarily in Chinese establishments, in large part due to cultural and linguistic barriers.[148]

Chinese Companies Active in Service Industry

Yi Lian Tang Chinese Clinic. Established by a Chinese entrepreneur with other business interests in Juba, the private clinic provides health services to "all the Chinese in town", as well as 50 to 100 South Sudanese per day. Its seven Chinese medical personnel and few local staff operate a laboratory, disburse medicines on site and will soon be equipped with x-ray and ultrasound capabilities. For an examination fee of 20 South Sudanese pounds (approximately $7), the clinic serves those who formerly travelled abroad for treatment of simple ailments. It reports that it was established primarily to fill this gap in health services, and its fiscal objective is only to cover costs.[149]

Beijing Juba Hotel. Opened in 2007, the hotel was among the first Chinese businesses in Juba, and its owner is one of the most widely-tapped resources for Chinese nationals in South Sudan. Despite two fires that destroyed much of its pre-fabricated accommodations, the hotel continues to reinvent itself. In recent months, the grounds have been transformed into a makeshift office park for expanding Chinese enterprises. In addition to the Chinese embassy, the property is now dominated by the temporary headquarters of Chinese-led oil consortiums, as well as some housing and office accommodation for CNPC, Huawei and a variety of Chinese companies fresh to Juba. New reception and restaurant facilities are under construction, and a transition back to hotel accommodation may follow, as management is concerned its commercial occupants may invest in more permanent locations.

V. OIL: TRANSITIONING SOUTH

China remains the dominant actor in the oil industries in North and South and the top buyer of their oil.[150] Its primary concern following partition remains the security of its oil assets, the vast majority of which now lie in South Sudan. Prior to separation, China invested billions of dollars in establishing the oil industry and importing more than 60 per cent of the country's crude.[151] Now, the Chinese-led oil consortiums are shifting their focus and operations south, while maintaining commercial cooperation with Khartoum – a balancing act that has proven no easy task.

After the signing of the CPA, oil production increased, fuelling economies in both North and South as a result of the agreement's wealth-sharing protocol, which divided proceeds between the two. Oil remained the centrepiece of the Khartoum-Beijing relationship but also played a new role in the previously neglected Southern regional capital, Juba. Given that the Chinese-operated producing fields are now primarily in the South and the chance to win new concessions there, oil will similarly occupy a principal position in Beijing's relationship with Juba.

As the CPA era wound down and the South's secession appeared increasingly inevitable, Juba reiterated the message Salva Kiir first delivered in 2007: that the oil was in the South and it was now time for China to re-orient its engagement. As an independent Juba gradually assumed control of its oil industry, it recommended that the oil firms and their operating companies (GNPOC and Petrodar) immediately establish new headquarters in South Sudan.[152] Juba's ministry was re-constituted, and the few Southern technocrats working in Khartoum came home to help

[146] One Chinese clinic has been operating for several years; a second is under construction and awaiting a government license.
[147] Crisis Group interview, Juba, November 2012.
[148] Crisis Group interviews, Juba, November 2001; Beijing, February 2012. "The records of Jeune Afrique's interview with Director-General Lu Shaye", Forum on China-Africa Cooperation (www.focac.org), 7 December 2011.
[149] Crisis Group interview, staff member, Yi Lian Tang Clinic, Juba, November 2011.

[150] Sudanese oil represented approximately 5 per cent of Chinese oil imports in 2010, according to the U.S. Energy Information Administration. "Country Analysis Brief: China" (www.eia.gov); CNPC reports that Sudanese imports accounted for 3 per cent in 2011. Crisis Group interview, Beijing, February 2012. The petroleum and mining ministry reports that UNIPEC and China Oil have been the two largest purchasers of South Sudanese crude. Crisis Group interview, Juba, November 2011.
[151] Some of the Sudanese oil purchased by China is subsequently sold on the international market.
[152] The Greater Nile Petroleum Operating Company (GNPOC) operates in blocks 1, 2, and 4. The consortium was owned by CNPC (40 per cent), Petronas (Malaysia, 30 per cent), ONGC Videsh (India, 25 per cent) and Sudapet (Sudan, 5 per cent). Petrodar operates in blocks 3 and 7; it is a consortium that includes CNPC (41 per cent), Petronas (40 per cent), Sudapet (8 per cent), Sinopec (6 per cent), and Tri-Ocean (5 per cent). Ownership shares remain the same today, save for Sudapet's, which in both cases were re-allocated to South Sudan's state-owned company, Nilepet. The details of this transfer remain a matter of dispute and may ultimately be submitted for international arbitration.

shape the South's own oil sector. Salva Kiir issued a presidential directive declaring Southern control of shares previously held by Sudan's state firm, Sudapet, and Juba began marketing and selling its oil – primarily to Chinese buyers – independent of Khartoum. Contact between CNPC and Juba increased, albeit discreetly.

In late 2011, as negotiations for an oil deal between Khartoum and Juba foundered dangerously, the role of China came centre stage, and many thought it would be forced to intervene. Beijing's delicate balance of relations was put to the test, as the South attempted to leverage Chinese majority interests in the South against Khartoum, and the impasse threatened a complete shutdown. At the same time, Juba and the Chinese-led consortiums were holding talks to renegotiate existing oil contracts previously held by Khartoum that now had to be transferred to the South. The interplay between the two sets of negotiations added another dimension to China's increasingly complicated position.

Given China's growing global options and the two Sudans' comparatively modest proven reserves, oil imports from North and South no longer occupy the significant position in China's global energy strategy they once did. But the considerable investments that have been made in developing and operating the oil sector mean that the Sudans will remain important for China and its state-owned oil giant, CNPC, in the short to medium term.

Chinese Companies Active in Oil Sector

China National Petroleum Corporation: CNPC is China's principal petroleum company, and among the world's largest corporations. Responsible for most oil and gas production at home and operating in 30 countries, it and its subsidiaries offer up- and downstream operations, field services and engineering construction.[153] Where necessary, operations are as closely integrated to the government as those of any state-owned enterprise.[154] The corporation has ministry-level status, and its general managers hold vice-ministerial rank,[155] meaning its representatives in effect outrank China's ambassadors in Khartoum and Juba. It has operated in Sudan since the mid-1990s and remains the dominant Chinese actor in North and South. It holds majority stakes, for example, in both of South Sudan's currently producing regions and led construction of and holds stakes in the Khartoum refinery, both pipelines traversing Sudan, and the export terminal at Port Sudan. Its numerous subsidiaries manage different aspects of the production process. Management has expressed interest in expanding into new concession areas in the South and building new oil infrastructure.[156]

Sinopec: China Petrochemical (Sinopec Group) ranks fifth on the Fortune 500 list of the world's largest corporations.[157] Established in 1998, the wholly state-owned parent corporation controls a series of subsidiaries and share-holding companies operating different parts of the production process. In Sudan, Sinopec International E&P Corporation Sudan Branch (SIPC Sudan) has a minority stake in Blocks 3 and 7 as part of the Petrodar consortium. Two other Sinopec subsidiaries have been primary petroleum engineering and servicing contractors in Sudan and participated in construction of the Petrodar pipeline.[158] Another Sinopec affiliate, China International United Petroleum & Chemicals Company (UNIPEC), is China's largest oil trader and the primary buyer of South Sudan's oil.

A. Renegotiating Oil Contracts

Negotiations between Juba and oil company partners – the largest stakeholder of which is CNPC – began soon after independence in order to transition existing oil contracts. Because there was "a new sheriff in town",[159] contracts that governed commercial arrangements with the Sudanese government had to be revised.[160] Oil contracts originally signed with Khartoum had to be brought in line with new political realities, as the terms pertained primarily to resources now belonging to the independent South.[161] Despite an initial sense that the talks would yield temporary "transitional" arrangements, the complexity of the negotiations and the broader political environment soon dictated

[153] Its businesses include "petroleum exploration and production, natural gas and pipelines, refining and marketing, oilfield services, engineering construction, petroleum equipment manufacturing and new energy development, as well as capital management, finance and insurance services", www.cnpc.com.cn.
[154] The line between government and state-owned enterprises is permeable and ill-defined, often a factor of personalities and circumstances.
[155] Crisis Group Report, *China's Thirst for Oil*, op. cit.
[156] Crisis Group interviews, CNPC officials, Juba, November 2011; Beijing, February 2012.
[157] "Global 500: our ranking of the world's largest corporations", *Fortune Magazine*, 25 July 2011.
[158] Sinopec International Petroleum Service Corp (SIPSC) is Sinopec Group's fully-owned international engineering and service arm. Zhongyuan Petroleum Exploration Bureau (ZPEB), another servicing subsidiary, previously reported more than 1,200 foreign employees in Sudan, more than half of whom were Chinese. "ZPEB's Sudan subsidiary", ZPEB (www.zpebint.com).
[159] Crisis Group telephone interview, official close to the negotiations, February 2011.
[160] Three contract areas were relevant: blocks 1, 2, and 4 operated by GNPOC; block 5A operated by WNPOC, and blocks 3 and 7 operated by Petrodar.
[161] There were considerable divisions within the SPLM leadership over how to handle existing contracts. While some asserted an extreme position of tearing up current agreements with the Chinese-led consortiums, in the end more pragmatic voices of those who hoped to adjust contracts but maintain continuity of oil operations prevailed.

that the agreements would in effect constitute new Exploration and Production Sharing Arrangements (EPSA). Both sides hired legal firms, and talks continued intermittently into December 2011.

South Sudan was in a position of some strength, though not an absolute one. Chinese companies developed and are operating the oil fields in South Sudan. While there are those who wished to see Western firms take the place of China and its partners, more pragmatic minds knew that was not realistic. The reputational cost of ripping up the contracts would have had drastic consequences for the new state's foreign investment profile.[162] Attempting to replace already established operations would have devastated the industry and the national budget and probably involved litigation that could prevent or stall any possible replacement. Thus, despite Juba's leverage, mutual interests dictated that the two parties would ultimately come to an agreement.

CNPC and its partners aimed to frame the negotiation in terms of a "continuation" of existing EPSAs.[163] Though Juba had made its commitment to protecting Chinese oil sector interests clear, it approached the talks with a view to "continuity of terms, not of contract". Mere continuation was unacceptable, as it denied the political reality of independence and ownership of its own oil sector. Furthermore, the opacity of contract arrangements, some associated loan structuring with Khartoum and the desire to improve some provisions demanded negotiation of "new" covenants. A senior official remarked that commitment to continuity of Chinese oil interests had indeed been made via a "gentlemen's agreement", but that did not constitute an oath to honour existing contracts without amendment.[164]

Juba was never fully abreast of the contract situation, as it remained without full access to the contracts themselves. It was also without the waivers and amendments agreed by Khartoum, such as those extending or waiving relinquishment obligations for unexplored concession areas. The South asked companies to divulge all such information, but because contracts between Khartoum and the companies are protected by confidentiality arrangements, the latter were reluctant to divulge what might violate their legal obligation. Juba explored legal recourse to secure the pertinent information (and possibly to provide cover to the companies), as the assets now belonged to the South. This included issuance of a presidential decree purportedly compelling disclosure. In the end, only a limited number of waivers and amendments surfaced, all of which were reviewed.

[162] Crisis Group interview, Sudan expert, Nairobi, December 2011.
[163] Crisis Group interview, CNPC official, November 2011.
[164] Crisis Group interview, cabinet minister, Juba, November 2011.

The most critical agenda item – the financial terms – was largely uncontested. Oil company anxieties eased considerably when the parties agreed to maintain the terms of the existing contracts.[165] It was also agreed that the prepartition ownership share distribution would remain the same among existing partners within the now wholly Southern-administered oil sector. The most substantive contractual changes were instead with regard to stronger environmental regulations, social protections, employment targets for South Sudanese nationals and transparency. Though an audit is not explicitly addressed in the contracts, there remains some desire to keep the idea of a full one – since production began – alive. CNPC expressed openness to an operational audit if conducted in light of historical standards, but not to a broader audit on social and human rights issues.[166] Though not a condition in the contracts themselves, Juba made clear that improving oil recovery rates would be a critical component of its new petroleum sector policy.

The original EPSAs contained a stabilisation clause: a mechanism designed to limit investor risk and preserve the value of the investment. Such clauses are particularly pertinent where stability is a concern and in industries that couple high up-front costs with a long-term return horizon. They permit companies to implement a contract under the legal framework that governed at the time of signature and commit host governments to compensate the investor if changes to that framework negatively affect the economic equilibrium of the venture or undermine its commercial viability.[167]

While honouring the cost implications of this investment protection, negotiators in Juba revised the stabilisation clause so as to avoid a scenario in which the threat of litigation or high compensation for improved standards would inhibit the adoption of strong regulatory legislation. If contractual changes to environmental, social, employment, or transparency standards yield economic consequences for the oil company, the consequent costs will be recoverable.[168] However, changes that concern the time value of money – eg, delays prompted by a mandatory environmental impact assessment – will not be cost-recoverable. The oil companies expressed reservations, but Juba was firm on revisions to the stabilisation clause as necessary to maintain flexibility in guiding its oil sector policy.

[165] Crisis Group interviews, oil consortia partners, petroleum and mining minister, Juba, November 2011.
[166] Crisis Group interview, Juba, November 2011.
[167] Lorenzo Cotula, "Regulatory Takings, Stabilization Clauses and Sustainable Development", OECD Global Forum on International Investment VII (2008).
[168] For example, if new requirements demand better lining of oil holding reservoirs to prevent ground water contamination, the cost of implementing those improvements will be recoverable.

The sequencing likewise proved relevant, as the centre of gravity of Beijing-Juba oil relations alternated between North-South talks on oil exploitation arrangements and contract review between Juba and the companies. At the most basic level, the new contracts themselves depend on Juba's ability to export oil. Juba hoped that some contractual clauses might influence the dynamics of North-South talks in their favour, including by either leveraging companies and new obligations against Khartoum, or providing the companies cover. Negotiators took two precautions to protect Southern interests against Northern intransigence. First, they encouraged companies to purchase the oil at the well-head, which would place the onus for transit fee arrangements on the companies and in effect remove Juba from the export equation. When that did not pan out, they began, as early as November 2011, to draft language that would protect the South should it decide to shut down its oil production.

Despite some perception that Juba's shutdown of oil operations was an emotional last-minute decision, a critical negotiated contract clause indicates otherwise. Article 19 of the new contract affords South Sudan's oil minister the liberty to "act with his or her complete and sole discretion", if Khartoum continued to confiscate oil, extort exorbitant fees or is otherwise obstinate. In the event of a shutdown, the clause freed the government from any liability or compensatory obligations to the companies. It also allowed absolute discretion to extend the contract with oil companies based on, among other things, their degree of cooperation in helping to resolve the impasse with Khartoum. The parties completed contract negotiations in late December 2011, and the companies agreed to the final document in principle, with one fundamental reservation: they asked the government to reconsider the power afforded by Article 19.[169] That clause further exposed them to hostile relations between the two governments, and as such they wanted full indemnification in the event of a shutdown and a guarantee of contract extension.[170]

Juba did not alter its position, and a high-stakes final hour ensued. On 13 January, CPC Politburo member Li Yuanchao arrived in Juba with a high-level Chinese delegation to discuss areas of cooperation and witness the signing of the new contracts with the Chinese-led oil consortiums. According to Southern negotiators, the Chinese submitted a series of revisions just hours before Li's arrival that amounted to full indemnity. They wanted to roll back much of what had been nominally agreed (including the discretionary rights outlined in Article 19 and revisions to the stabilisation clause) and achieve an agreement that all oil would continue to be exported through Northern infrastructure. They hoped to leverage Li's visit and the economic cooperation on offer. South Sudan refused, the Chinese relented, and the signing ceremony went ahead, confirming the contracts as endorsed in December.[171]

B. Restructuring and Relocation

Partition prompted not only contract revisions, but also restructuring and relocation of existing operations. Southern officials were frustrated that the Chinese were slow to re-orient their activities southward after 9 July 2011, arguing they "cannot serve two masters", but the Chinese were hesitant to move as long as the safety of their investments seemed still in question.[172]

Oil blocks 1, 2 and 4 – together the most lucrative since the CPA – are operated by Greater Nile Petroleum Operating Company (GNPOC), a consortium of four oil firms led by China's CNPC. Partition has proven particularly complicated for GNPOC, as its concession spans the North-South border. Despite warnings by its owners and international advisers, Southern officials made clear they wanted a division of the consortium and an independent Southern operation rather than a joint cross-border arrangement. Cognisant of a not yet firm relationship, the companies were reluctant to object too strenuously. But their displeasure and the strain of the transition are evident and have been complicated by the North-South crisis.[173] The joint operating company is forced to mirror the delicate balancing act of its managing partners; an official close to the transition lamented that the split-up of GNPOC was ill-advised and argued "nobody has the guts" to challenge Juba's decision.[174]

GNPOC established a presence in Juba in June 2011, though with only a single manager and a few support staff, who served as liaison between the Southern government and GNPOC headquarters in Khartoum. It has acquired a building in Juba and will begin refurbishing it with the aim of staffing a new headquarters – reportedly with up to 200 staff – though the timeframe remains uncertain.[175] The existing management structure is likely to be duplicated in a separate operating entity in the South: a CNPC president, a national vice president, and operations, pipeline, and administration managers from the partner companies. Beyond an executive structure, the lack of trained staff in

[169] Crisis Group interviews, members of Juba's negotiating team, Addis Ababa, January 2012. Crisis Group telephone interview, official close to the negotiations, February 2012.
[170] The companies requested that contracts be extended for a time period equivalent to the duration of the shutdown. Crisis Group interview, Beijing, February 2012.
[171] Crisis Group interviews, GoRSS negotiators, Addis Ababa, January 2012.
[172] Crisis Group interviews, cabinet ministers, oil company officials, Juba, November 2011.
[173] Crisis Group interview, GNPOC official, November 2011.
[174] Crisis Group interview, Juba, November 2011.
[175] Crisis Group interview, GNPOC official, November 2011.

the South remains a priority concern. Petrodar likewise scaled up its presence in Juba, though to the chagrin of the government not until January 2012.

As per Juba's insistence, CNPC also established a small office; its ten staff provide support to its operating companies, and will be scaled up to fifteen. A series of CNPC subsidiaries responsible for exploration, engineering, construction, and drilling have also transitioned south, though they have been largely idle since the shutdown. Like the embassy, both oil consortium headquarters and several other Chinese outposts, CNPC's temporary headquarters was on the grounds of the Beijing Juba Hotel, though it has recently acquired new space elsewhere. CNPC officials note they have not just arrived, touting the computer lab the company constructed at Juba University and opened in early 2011, training and study tours for oil ministry officials in years past and a previous commitment to establish a petroleum engineering department at Juba University.[176] The petroleum ministry hopes China will train additional professionals once capacity gaps are identified. Juba would be wise to seek employment quotas for non-skilled positions as well, in order to maximise the number of nationals employed in the sector.

C. New Concession Areas

The petroleum ministry is revising concession areas. Current blocks were negotiated and sized during the war. The territory will be divided into new numbered blocks, opening up new areas and resizing current blocks that far exceed international norms.[177] Guidelines for the size of new concession blocks will be set to ensure areas "large enough to secure industry interest and a competitive process", but not so large as to exceed "what can be effectively explored during the license period".[178] Currently producing areas will not be affected, but ministry officials report that unexplored blocks, as well as unexplored portions of producing blocks, may also be sub-divided and new licenses issued.[179] CNPC asserts that this should only be permissible if relinquished by the company in line with the terms of the existing contracts, though the law may supersede contracts in the end.[180]

CNPC, Sinopec, and other Chinese oil companies have expressed interest in exploring new concession areas, but further feasibility studies are necessary. CNPC has also held discussions with Total, which holds rights to the largest unexplored block in South Sudan and is seeking minority partners. Company officials acknowledge that future oil discoveries may be limited, but they remain interested in securing the right to find out. Many Southerners dismiss conservative estimates, though such opinions are not often based on technical forecasting.[181]

Some SPLM officials are adamant that Juba place strict limits on the number of new concession areas awarded to Chinese companies so as to prevent a monopoly and have promoted this policy line within the party's political bureau.[182] This may be wise policy, but even those most concerned acknowledge that because U.S. and other Western oil majors are hesitant to re-enter the market – sentiments reinforced by the shutdown – maintaining such quotas in oil and other investment sectors will prove difficult.

Discussions have also prioritised boosting oil recovery rates that reportedly average 20 to 30 per cent in producing areas. Ministry officials want to lift these to 40 to 45 per cent, which industry experts report is possible.[183] Some in the petroleum servicing sector argue that technology is available that can "dramatically extend the life of current reserves".[184] Recovery rates are likely to be given greater scrutiny in the annual work plans submitted for approval by operating companies, which include technology standards. New petroleum servicing companies will compete with current contractors to meet the desired standards in new and existing concession areas.[185]

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[176] The establishment of such a department has not progressed, due in part to funding problems that have stifled university operations in recent years.
[177] The draft petroleum bill retains the right to re-designate existing blocks in producing areas, and the existing contracts will be amended accordingly.
[178] "Petroleum Policy, Draft", GoRSS, December 2011.
[179] The ministry wants to give companies only six years to bring blocks into production. Section 26.1 of South Sudan's draft petroleum bill (obtained by Crisis Group) states: "Petroleum agreements shall provide for an exploration period not exceeding six years from the effective date of the agreement".
[180] Crisis Group interview, Chinese oil company official, Juba, November 2011. Crisis Group telephone interview, oil industry expert, February 2012.
[181] Oft-cited forecasts from industry experts project a dramatic decline in oil output in ten to fifteen years.
[182] Crisis Group interview, cabinet minister and SPLM politburo member, Juba, November 2011.
[183] Crisis Group interview, Petroleum Minister Stephen Dhieu Dau, Juba, November 2011. Actual recovery rates vary dramatically between countries and blocks based on a variety of factors, including field type, technical sophistication, economics and the employment of secondary and tertiary enhanced oil recovery methods. Crisis Group email correspondence, U.S. Energy Department official, January 2012.
[184] Comments by U.S.-based petroleum servicing company executive, U.S.-South Sudan Engagement Conference, Washington DC, 15 December 2012.
[185] Chinese and French servicing companies lead those currently active; Halliburton is among the Western companies that have demonstrated an interest in bringing new technology to South

D. New Oil Infrastructure

As the prospect of an oil shutdown mounted in January, the option to build an alternative export pipeline returned to the fore. Oil located in the South was historically moved through two pipelines: one beginning in the Muglad basin from blocks 1, 2, and 4 (GNPOC), and one beginning in the Melut basin servicing blocks 3 and 7 (Petrodar). Both traverse the North and empty at its Port Sudan on the Red Sea. Plans for an alternative pipeline have been talked about for decades; numerous options are under consideration, most of which are destined for seaports in Kenya or Djibouti (via Ethiopia).

Because the quantity of South Sudan's reserves remain unknown, such a pipeline has been subjected to considerable scepticism. Some petroleum experts argue that currently proven reserves alone would not provide economic justification for a project that would cost billions of dollars and take several years to complete. But as Khartoum continued to demand exorbitant transit fees and began to divert Juba's oil in late 2011, the cabinet accelerated pursuit of a pipeline project and welcomed new proposals. The government also signed memorandums of understanding with Kenya, Djibouti and Ethiopia on construction of a pipeline and began seeking financiers.[186] The proposed route through Kenya to a new deep-water port at Lamu has received the most attention, though much remains to be studied, and no deals have been struck.[187]

Despite considerable buzz about Chinese interest in building an alternative pipeline, as well as the proposed port in Lamu, Chinese officials noted in late 2011 that no decision had been taken.[188] At least one Chinese company had expressed a concrete interest in the pipeline project by then, and others were showing interest as it again became a priority. Prior to the crisis, CNPC was willing to provide technical and economic assessments of a pipeline project and had indicated willingness to participate in construction should Juba choose to go forward. CNPC also affirmed South Sudan's desire to attain refining capacity, arguing a refinery that would complete the chain of up- and downstream activities was in the nation's interest. While Chinese companies are among the many who have submitted proposals to build refineries, potentially lucrative oil infrastructure projects have sparked interest from companies around the globe.

However, the oil crisis has altered Chinese equations on a pipeline, at least in the near term. As Juba's desire to build one accelerated, some worried that progress toward a pipeline could become a disincentive to continue negotiating with Khartoum. The end of negotiations and an alternative pipeline would essentially render obsolete the Northern pipelines, which are wholly or partially owned by the oil consortiums and whose cost has not yet been recovered.[189]

CNPC also raised concerns with Juba about the challenge it would face in recovering costs of construction, the time required and the troubles of building on difficult terrain, as well as the possibility that new processing and export infrastructure could exceed the cost of a reasonable transit fee arrangement.[190] However, if it becomes clear that the government has prospects to finance a pipeline project, CNPC calculations may evolve, and Juba may attempt to induce Chinese participation.

Sudan. Crisis Group interviews, U.S. official, senior South Sudanese petroleum official, Washington DC, December 2012.

[186] Lucas Barasa, "Kenya, South Sudan sign oil pipeline deal", *Daily Nation* (Kenya), 25 January 2012. The memorandum of understanding with Kenya also committed the two parties to negotiate transit fees based on international norms. Salma El Wardany and Mohamed Osman Farah, "South Sudan, Ethiopia sign accord on Djibouti oil pipeline", Bloomberg, 9 February 2012.

[187] A joint technical committee of South Sudanese and Kenyan officials held talks in February to discuss Kenya's role, as well as transit fees, security, immigration, and pipeline management. Kenya hopes such a project would open another transport and economic corridor, linking it with South Sudan and Ethiopia, and thus solidify its position as the primary hub of economic activity in the region. "Lamu abuzz with construction as South Sudan seeks new pipeline", *The East African*, 11 February 2012.

[188] Crisis Group interviews, Nairobi, November 2011.

[189] The Petrodar pipeline remains wholly owned by Petrodar but is due to be transferred to government ownership in 2017 after costs are fully recovered. Though it retains a minority stake, GNPOC has in effect transferred majority ownership to Khartoum; full ownership transfer will be completed in 2014. "Annual report 2010-2011", ONGC, 2011, p. 221, at www.ongcindia.com. Loss of the combined outstanding value could ultimately prove acceptable to the companies, though it is not desirable.

[190] Crisis Group interview, Beijing, February 2012.

VI. NORTH-SOUTH DEADLOCK: CHINA DRAWN INTO OIL CRISIS

Some nine months beyond partition, negotiations between Khartoum and Juba have yet to yield an arrangement on the export of Southern oil, imperilling both economies and prompting renewed rhetoric of war. Roughly three quarters of the remaining oil now belongs to the South, but the infrastructure to exploit it – pipelines, refineries and export terminals – are in the North. Between November 2011 and February 2012, the parties convened three rounds of negotiations in Addis Ababa to forge a deal on oil and transitional financial arrangements. Partition, with the resulting loss of its main revenue stream, meant Khartoum was facing an economic crisis. Juba would have to pay transit fees since its oil was crossing Sudan's territory en route to market. Given previous commitment to the concept of two mutually viable states – a basic principle of the negotiations – Juba would be asked for more so as to soften the blow. While oil headlined the talks, the need also to agree on arrangements regarding debt, security and proxy conflict, borders, and the disputed Abyei region added layers to an already complex negotiation.

Dramatically different proposals, heightened hostilities along the border, brinkmanship and dangerous unilateral actions reinforced mistrust, caused the talks to end without agreements and ultimately led Juba to shut down its oil production. The international community – including China – was worried by the high-stakes poker game, and Beijing's multi-billion dollar investment and energy supply needs meant it had particular cause for concern. Referring to the increasingly uncomfortable position of the Chinese oil companies and their partners, a South Sudanese negotiator cited an African proverb: "When two elephants fight, the grass suffers".[191]

Both sides hoped the Chinese might weigh in on behalf of a deal, though Beijing's influence, and readiness to employ it, appeared to be over-estimated. Such over-estimation was common not only in the two Sudans, but also among the wider international community. Months earlier, before the crisis peaked, China's ambassador to Juba, Li Zhiguo, argued that external inputs would be counterproductive, and China would not intervene with proposals or suggestions, "because the issue is an internal affair of the two brothers of Sudan".[192] In the interest of a deal, Beijing's envoys stretched the interpretation of non-interference in the challenging months that followed, but China's careful approach was dictated by its explicit desire to maintain balanced relations with North and South.

A. Negotiating Positions and Khartoum's Gamble

During talks in November 2011, the African Union High-Level Implementation Panel (AUHIP), tasked by the regional body to resolve outstanding issues between Sudan and South Sudan, submitted a new compromise proposal to the parties. It included $2.6 billion to be paid by Juba to Khartoum, over four years, to help cover one third of the North's coming revenue gap.[193] Khartoum would cover another third through austerity measures, and the international community would pitch in the remaining third.

Juba accepted the proposal in principle and offered to forgive an additional $2.8 billion in arrears owed it by Khartoum, for a total package of $5.4 billion – more than 70 per cent of the revenue gap.[194] Regarding transit fees for transport of the South's oil across Northern territory, Juba would offer 74 cents per barrel for oil flowing through the GNPOC pipeline and 66 cents per barrel for oil through the Petrodar pipeline, in perpetuity.[195] Juba also pledged to soften its earlier position that a financial package be conditioned upon immediate transfer of Abyei to the South; complete demarcation of agreed areas of the North-South

[191] Crisis Group interview, Addis Ababa, November 2011.

[192] Li noted, "Any intervention in this key sector from the outside would only complicate the situation and would not help resolve the issue … we will respect the decision by the two sides and adjust our plans of cooperation accordingly". "China trains petroleum workers in South Sudan", Xinhua, 11 July 2011.

[193] The revenue gap as calculated by the IMF over a four-year period, 2011-2015, was $7.7 billion. Crisis Group interviews, Addis Ababa, January 2012.

[194] The discussion of arrears continues between North and South, with no agreement on the estimated $5.8 billion Juba claims it is owed in unpaid or misused oil revenue of various kinds, unpaid and future government pensions for South Sudanese and a series of other CPA-era fees.

[195] Its transit fee figures were derived from cost-based transit fee calculations using the example of the Chad/Cameroon oil pipeline (41 cents per barrel) and taking into account the distance of the two pipelines traversing Sudan. The GNPOC pipeline begins in the Unity state fields and traverses Heglig and Khartoum before continuing some 1,600km to Port Sudan on the Red Sea. It is operated by CNPC. The government has a 70 per cent stake in the pipeline; the remaining 30 per cent belongs to GNPOC partners. Petrodar owns and operates the pipeline that begins in the Melut basin of Upper Nile state, stretching some 1,500km to Port Sudan. Juba later adjusted its calculations to 69 cents and 63 cents per barrel for the respective pipelines, before ultimately offering one dollar for both. Negotiations were fluid and in each round involved a series of proposals, counter-proposals and compromise options. Juba's negotiators initially signalled that transit fee arrangements should replace – not complement – the $2.6 billion cash transfer on offer, though in later rounds of negotiations, they said that transit fees, if agreed, could be deducted from the $2.6 billion grant over the course of the initial four-year period.

border; and Khartoum relinquishing claims on the contested border areas. [196]

Khartoum based its counter-proposal on its own calculation of a significantly higher revenue gap of $10.4 billion; it wanted the South to contribute $7.4 billion toward covering that gap over four years.[197] It expressed reservations about the provision in the AUHIP plan for the international community to cover one third, citing past commitments it felt had not been kept and its continued lack of trust. Western officials hoped China might finance, or take the lead in securing, this one third, as that would enable Beijing to positively impact the negotiations and potentially curry favour with both North and South.

When AU mediators floated this idea, the Chinese initially expressed some reluctance. Chinese officials later noted, however, that their government has not been formally asked to cover the remaining gap, and some in Beijing believe that if Khartoum agrees to the package, China would be open to providing a portion of it.[198]

Such considerations come in the context of a broader landscape of economic cooperation with Khartoum. China has extended preferential credit to Khartoum since development of the oil sector accelerated in the mid-1990s. By the beginning of 2010, Sudan owed it at least $1.9 billion.[199] Beijing continued to extend credit and in January 2012 offered another concession by suspending Sudan's repayments for five years.[200] Lending money was commercially sound when Sudan was producing oil, but without the oil, China must now consider whether "lending" more money might in effect mean "giving".[201]

China is more willing to extend credit to indebted countries where there is a political imperative.[202] Sudan sought additional funds from its Exim Bank in 2010 but was denied in view of the uncertainty about the referendum and potential instability caused by separation. Khartoum's negative financial outlook may also prompt greater caution, but Beijing's development banks report that China's long presence in, and familiarity with, Sudan means they are likely to continue to finance new ventures outside the oil sector as long as they are commercially viable.[203] Some in Beijing assert that despite dwindling resources in Khartoum, there is sufficient political justification to continue extending credit.[204] China is unlikely to abandon an old political ally with whom its relationship goes back decades.[205] That Sudan was the first site of China's "go out" policy also gives the country symbolic importance, particularly with senior leaders who were personally involved in early operations.[206]

In contrast to Juba's offer, the Khartoum plan proposed transit, central processing, marine terminal, and transportation fees totalling $36 per barrel.[207] This was deemed far too high by international observers and Southern negotiators alike. The latter argued the transit fees were inconsistent with international practice, and the other fees demanded were already being paid, per contractual arrangements governing the infrastructure, to the oil companies themselves. Juba also complained that the North's negotiators had a figure in mind they hoped to extract from the South and would manipulate their proposals however necessary to secure it. Khartoum countered that South Sudan has no investment of its own in already functioning pipelines, refineries and export terminals and is not a party to the agreements governing their use; thus, any cost calcu-

[196] "Response to the Proposal of Sudan on Crude Oil Multiple Transportation Fees and RSS/SPLM Principled Position", RSS Power point presentation, 28 November 2011; Crisis Group interview, international adviser, Juba, November 2011.
[197] Crisis Group interviews, NCP officials, Addis Ababa, November 2011.
[198] Crisis Group interviews, Beijing, February 2012.
[199] Actual debt to China is thought to be greater than what has been reported. Crisis Group email correspondence, Sudan oil sector expert, January 2012. In addition to oil infrastructure, the Chinese government has financed billions of dollars of major dam projects, roads, railways, power, water and other major infrastructure projects in Sudan.
[200] The deferment was announced during the January visit of Li Yuanchao to Khartoum. Li also offered a concessional loan of $200 million for "various development projects". "China Defers Loans Payable by Sudan", *Sudan Vision*, 15 January 2012. The concession that the North would not have to make repayments for five years was in effect a recognition of reality, since Khartoum was unlikely to have been able to do so in any event.
[201] Crisis Group interview, international economist, Addis Ababa, January 2012.
[202] An April 2011 white paper from China's State Council News Office entitled "China's Foreign Aids" reported that China issued 256.29 billion RMB in foreign aid ($40.5 billion) and has signed agreements exempting roughly 10 per cent of that total sovereign debt. "China's Foreign Aid", April 2011.
[203] Crisis Group interviews, Beijing, Shanghai, February 2012.
[204] Crisis Group interviews, foreign policy experts, Beijing, Shanghai, February 2012.
[205] Crisis Group interviews, Beijing, November 2012.
[206] Crisis Group Report, *China's Thirst for Oil*, op. cit.
[207] The $36 proposal included transit ($6 per barrel), central processing ($5 per barrel), marine terminal ($6.50 per barrel) and transportation fees ($18.50 per barrel). In calculating transit fees, Khartoum also used the Chad-Cameroon pipeline as a baseline, but adjusted for current oil prices. Juba argued that no precedent merited such cost adjustment anywhere in the world. "Crude Oil Multiple Transportation Fees Proposal", Sudan petroleum ministry presentation, November 2011. Fee estimates were later adjusted by Khartoum to $32.20 per barrel.

lations based on those agreements are irrelevant.[208] The parties showed little willingness to budge from their positions, casting a shadow over prospects for a deal.

As the talks foundered, Southern oil officials reported on 30 November that Khartoum had delayed at Port Sudan the loading of a 600,000-barrel shipment of oil belonging to the South and sold to China's UNIPEC. The unilateral move was perceived as an attempt to force Juba's hand at the negotiating table. Though Juba was outraged and made clear it would not respond to such pressure, negotiations in Addis Ababa continued. A second shipment of Southern oil (one million barrels sold to the Geneva-based fuel trader Vitol) was likewise delayed on 3 December.[209] Khartoum's oil minister confirmed Southern exports would be stopped until a deal was reached, and Northern officials later asserted that the shipments had been confiscated in lieu of payments owed by South Sudan for oil exports since July. Given limited holding capacity, shipments could only be delayed for a matter of days, after which the crisis would reach a dangerous climax, as production might have to be stopped.

B. China is Drawn in

As the tension ratcheted up, China was drawn in. Upon hearing of the blocked oil exports, Beijing's ambassador to Khartoum, Luo Xiaoguang, took a rare public position, calling the move "very serious and unjustified".[210] Juba was increasingly unhappy that China, the principal third-party involved in the oil sector, was not playing a more active role in breaking the deadlock. As the crisis developed, a senior minister noted that "as things stand now, the relationship is not warm between us and China".[211] If China was reluctant to demonstrate its commitment to the relationship with the South, then Juba would seek to leverage Beijing's increasingly uncomfortable position.

On 1 December, senior government officials summoned Chinese oil company representatives in Juba to deliver three messages. First, the companies would be expected to weigh in with Khartoum to convince the authorities there that their transit fee proposal was unreasonable. Secondly, the arrangement just devised by Khartoum – in which oil belonging to the South was prevented from loading, but oil earmarked for the Chinese would continue to be exported – was unacceptable. This was a veiled threat that if China was passively complicit in such a scheme, Juba would ensure that "all three parties would lose"; moreover, South Sudan might be "forced to rethink the EPSAs", a targeted jab given that the Chinese remained concerned about ongoing negotiations to renew existing oil contracts with the South.[212]

Thirdly, relations with any company buying "stolen" oil would suffer or be ruined. This was reiterated to all potential crude purchasers in a press release, which noted that the government reserved "all of its rights, including the right to take legal action against anyone buying directly or indirectly, or anyone handling, shipping or otherwise dealing with" confiscated oil from South Sudan. Complicity would not be tolerated.[213]

In response to the démarche, the company representatives immediately asked that senior executives come from Beijing to address the issues at a higher level. More visibly, the crisis prompted a visit from China's special envoy for African affairs, Liu Guijin, who had last come to Sudan in June 2011, to encourage an oil agreement.[214] The Chinese report that in subsequent months they had consistently urged restraint and maintained that Liu would return if critical circumstances demanded so.[215] In early December, Liu returned to reiterate the message, urging compromise on both sides and noting a failure to agree would mean "the whole region would be affected, the repercussions would be very serious".[216] Liu encouraged the parties to accept the interim AU proposal then on the table and sought verbal commitments that neither side would take further unilateral action.[217] But the commitments would not hold for long. Simultaneously, both sides expanded attempts to leverage China's interests.

While greater Chinese efforts were warmly welcomed, senior diplomats close to the process and other observers expressed disappointment in the relatively shallow character of the engagement. Given limited international leverage

[208] Crisis Group interviews, NCP officials, SPLM officials, Addis Ababa, November 2011. "Response to RSS Presentation of 28th Nov, 2011", NCP PowerPoint presentation.
[209] Salma El Wardany and Jared Ferrie, "China's Africa Envoy will Head to Sudan to Push Oil Talks", Bloomberg, 5 December 2011.
[210] "Pipeline Problems", *Africa-Asia Confidential*, vol. 5, no. 2, December 2011.
[211] Crisis Group interview, cabinet minister, Juba, December 2011.
[212] Ibid.
[213] Petroleum and mining ministry, press release, 1 December 2011.
[214] The Chinese government also attempted to bring Presidents Bashir and Kiir together in Beijing in 2010 and 2011, to no avail.
[215] Crisis Group interviews, Juba, November 2011.
[216] "China urges Sudan and South Sudan to break oil deadlock", *Sudan Tribune*, 12 December 2011.
[217] In Khartoum, Liu met with a group of senior officials headed by Vice President Ali Osman Taha. In Juba, he met the oil and foreign affairs ministers, then President Salva Kiir. The Southern leadership expressed its disappointment that it was being treated like a province rather than an independent state. Crisis Group interviews, government officials, Juba, Washington DC, Beijing, December, February 2012.

with the parties (Khartoum in particular), they encouraged Beijing to cultivate a deeper understanding of the negotiations and the positions of the parties, so as to exert influence where possible.[218] The Chinese envoy did engage his U.S. and UK counterparts, requesting that they help in pressuring Juba to compromise, while China would do what it could with Khartoum.[219] But Western officials remained unconvinced as to how active or successful China was in persuading the NCP.

Beijing's aversion to interference and its desire to maintain balanced relations were not fully appreciated by Sudanese or international actors. But Chinese experts and officials in Beijing acknowledge the government should and could do more without compromising on non-interference, citing its role in facilitating the entry of UN peacekeepers into Darfur as well as previous attempts to convene a meeting between Presidents Bashir and Kiir in Beijing.[220] They deem reasonable the request by international counterparts to be more actively and consistently involved in North-South negotiations. Some argue China is now in a difficult position precisely because of insufficient engagement and argue: "We are bystanders; we cannot just be bystanders, we need to be a player. Can you imagine how any Western country would engage if they had all these interests?"[221]

Nevertheless, serious impediments remain, including lack of experience in direct mediation, insufficient capacity, and the relatively weak position of the foreign ministry within the party and overall government structure.[222] One official remarked: "It will take time for China to adapt its diplomacy to reflect the global status we now enjoy".[223] After five years as special envoy, Liu retired in February 2012; Chinese efforts will be taken forward by his successor, Zhong Jianhua, who made his first visit to Sudan and South Sudan in March.[224] It is hoped that this opportunity will be taken to strengthen support to the special envoy.[225]

C. Oil Companies Appeal for Restraint

When talks re-convened in January 2012, the atmosphere had again been tainted by unilateral action, and the brinkmanship promptly resumed. In the absence of a deal, Khartoum blocked several more shipments of Southern oil reportedly valued at more than $140 million.[226] At the demand of Sudanese security forces, oil operators were forced to load two shipments of oil owned by the South onto ships chartered by Khartoum, and another was unlawfully diverted to its refinery.[227] The purported justification was again that Juba owed Khartoum fees for oil exported in the absence of an agreement.

Representatives of the oil companies were invited to join the parties in Addis. Juba requested they confirm that transportation and processing fees were in fact being paid. The companies did so, including in writing, thus undercutting Khartoum's claims.[228] For a senior member of Juba's negotiating team, this new cooperation was a direct result of the new contracts that were signed with South Sudan, which they believed brought company interests more in line with their own.[229] The companies, led by CNPC representative Sun Xiansheng, also made presentations on the many technical problems resulting from the impasse, such as conflicting orders yielding irregular lifting schedules and inefficiencies; difficulty in moving personnel and supplies across the border; and insufficient staffing in the South. The impasse also meant oil tankers docked at Port Sudan waited, at considerable cost, well past their scheduled loading dates.

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[218] Crisis Group interviews, Addis Ababa, Washington DC, January 2012.
[219] Crisis Group interviews, U.S., UK officials, Washington DC, December 2011-January 2012, Beijing, February 2012.
[220] Crisis Group interviews, Beijing, November 2011 and February 2012.
[221] Crisis Group interview, Beijing, February 2012.
[222] For example, requests by high-level Chinese officials to travel encounter internal bureaucratic impediments. The difficulties the foreign ministry faces in playing a stronger role include the lack of technical knowledge among Chinese diplomats regarding the oil disputes, the limited number of Chinese diplomats on the ground and the fact that the heads of Chinese oil companies enjoy ministerial status, thus outranking the special envoy.
[223] This sentiment was echoed by other foreign policy experts in Beijing; one called the foreign ministry "a little detached" when it came to the details. Crisis Group interviews, Shanghai, Beijing, February 2012.
[224] Zhong's initial engagement is detailed further below.
[225] Zhong was most recently Chinese ambassador to South Africa, a post also previously held by Liu Guijin. In addition to Pretoria, Zhong has undertaken assignments in the UK, Beijing, the U.S., and the former Yugoslavia. "H.E. Zhong Jianhua", Who's Who Profile, *Africa-Asia Confidential*, undated.
[226] "Government of Sudan poisons negotiation atmosphere in Addis by stealing 1.4 million barrels of South Sudan oil just days before", press release, GoRSS, 17 January 2012.
[227] Letters from Dr Liu Yingcau, president of Petrodar Operating Company, addressed to South Sudan Petroleum Minister Stephen Dheiu Dau, 13 and 16 January 2012, obtained by Crisis Group.
[228] Letter from CNPC, PETRONAS, and ONGBV addressed to petroleum ministers from Sudan and South Sudan, 3 January 2012, obtained by Crisis Group.
[229] For example, when Khartoum later began to confiscate or divert oil belonging to the South, the oil companies cooperated in documenting and communicating as events unfolded, something that would never have happened when Khartoum was in control of the oil sector.

The companies demonstrated their concern by also addressing the ramifications of a shutdown and did what they could to try to keep the oil flowing. In addition to the proposals tabled by the AU mediation, they offered an informal suggestion to help avert a crisis in the interim: a $600 million package for Khartoum in the form of crude oil, of which one quarter would be borne by the companies and three quarters by Juba. With regard to any credits, including those previously offered by the Chinese, the North preferred crude rather than cash, so as to maximise use of its physical and human capital, most notably by keeping the Khartoum refinery operating at full capacity. Amid the flurry of changing positions and proposal amendments, the companies' offer to contribute was considered but not taken up specifically.

D. Juba's Oil Sector Shutdown

The series of proposals and counter-proposals that the January round featured failed to bridge the divide. However, the mediation attempted to keep the parties talking at least until the AU summit, at month's end, as they hoped high-level multilateral engagement might prompt a breakthrough. Meanwhile, Juba had commenced a shutdown, preferring, as it saw matters, to fully exercise its economic sovereignty than be held financially hostage by Khartoum. Though a lengthy shutdown would have grave consequences for the national budget and investor confidence in the near term, Juba preferred to prepare for deep budget cuts and pursue external support while accelerating the construction of a new export pipeline. Meanwhile, its oil would remain in the ground, possibly for several years. Kiir briefed the national assembly, which endorsed the decision, and other preparatory actions were taken. Given the financial ramifications on Juba's oil-dependent economy, many viewed the move as a bluff, but they would soon be proven wrong.

Beijing continued to appeal for restraint and dialogue. Officials close to the talks report the CNPC leadership also urged President Bashir to release the tankers holding South Sudan's oil, hoping that would prompt Juba to agree to an interim arrangement. But the chances were slim that release of the stolen oil alone could be a catalyst for a deal, particularly in the absence of assurance that Khartoum would not again resort to diverting Juba's oil.[230]

As the prospect of a full shutdown loomed, the annual AU summit brought Presidents Kiir and Bashir together. Ethiopian President Meles Zenawi and Kenyan President Mwai Kibaki joined the AUHIP's Thabo Mbeki in mediating, but the most recent iteration of the AUHIP proposal had changes Kiir found too drastic to accept. These included a proposed transfer of $2.6 billion to $5.4 billion (to be negotiated) to Khartoum, to begin immediately in the form of crude oil; a $3 transit fee; and a requirement to use Sudan's pipeline infrastructure, while deferring resolution of both confiscated oil repayments and arrears to subsequent time-bound negotiations. Southern negotiators considered both that the price was too high, and the proposal would not sufficiently bind the parties to a course toward a comprehensive settlement. Given that Juba's cabinet and national assembly had supported the rationale for the shutdown, such a deal would in any event have been a politically difficult sale at home. The shutdown was completed at the end of January.

Both sides again engaged the Chinese. President Kiir met in Addis Ababa with Foreign Minister Yang Jiechi, who hoped for a reversal of the drastic development and cautioned on the ramifications of a shutdown for CNPC operations. Kiir responded that South Sudan's national interest came before those of any investor and asked what guarantee China could provide to ensure the safety of Southern oil exports.[231] Meanwhile, a senior CPC figure, Jia Qinglin, met with President Bashir at Khartoum's request also to discuss the shutdown. The North, likewise seeking to pull China into its corner, reported it had called on Beijing to pressure South Sudan and publicly claimed that Bashir was assured of support for Sudan's position in the negotiations – an unlikely commitment in light of China's desire to maintain a balanced stance.[232]

The parties re-convened in Addis Ababa in February, but the threats and recriminations that followed the failure of the January talks had created a poisonous environment that made a deal unlikely. Juba meanwhile began to introduce austerity measures to drastically cut government expenses, and tensions with China continued to mount.

Southern officials reported that during the shutdown, a greater number of wells were found in several producing fields than had been previously recorded. They accused Khartoum of again under-reporting oil output, and Petrodar – and its Chinese and Malaysian parent companies – of complicity. Petrodar denied wrongdoing, explaining the discrepancies were a result of water separation during pumping.[233] But the mistrust came at the height of tensions over the shutdown and compounded Southern anger that the company had been too slow to re-orient and solidify its relationship with the new state. Complaints included delayed relocation of Petrodar headquarters to Juba, un-

[230] Crisis Group email correspondence, international officials, February 2012.

[231] Crisis Group telephone interview, meeting participant, February 2012.
[232] "Sudan urges China to exert pressure on South Sudan to reach oil deal", *Sudan Tribune*, 29 January 2012.
[233] Hereward Holland and Ulf Laessing, "Oil risks fuelling flames of Sudan conflict", Reuters, 3 February 2012.

warranted cooperation with Khartoum, and a dispute over the future of a minority consortium share previously held by Khartoum's national oil company. The grievances prompted the oil minister to issue a 20 February order expelling Petrodar's Chinese president, Liu Yingcai, from the country. The Chinese expressed displeasure via diplomatic channels, and the incident added to friction between the new partners and growing anxiety among Chinese nationals in Juba.[234]

E. A Possible International Entry Point?

North-South talks convened again in March. Though few had hopes an oil deal would materialise, the parties did agree in principle to shift the focus of oil negotiations. Rather than continue to attack each other's proposals and haggle over Juba's contribution to Khartoum's coming revenue gap, negotiators decided to focus instead on the role the international community could play in covering that gap. The South's chief negotiator circulated a letter to that end, and the idea was welcomed by the North's negotiators as well as the AUHIP and other international partners.[235]

Within weeks, however, dangerous North-South border clashes threatened to undermine the apparent progress and the talks more broadly. If the sides can avoid escalation and reclaim a collaborative approach to this agenda, it could set the stage for China and other partners to help break the deadlock, assuage mutual anxieties with Juba and restore an environment in which relations can continue to thrive. Financial support and a deal on oil could help prevent economic collapse in one or both states in the near term, but care must be taken as to how financial assistance is offered lest it reinforce negative political dynamics and simply defer the problem.

In addition to China, a number of Arab states are reportedly being consulted as potential financial contributors, notably Qatar, Kuwait, and Saudi Arabia.[236] Though the U.S. and other Western states are unlikely to contribute money, they support the plan for filling the revenue gap. Rather than a free bailout to Khartoum, they would prefer funding to be leveraged against a deal for oil, humanitarian access and a political process in Southern Kordofan and Blue Nile, as well, possibly, on resolution of other outstanding issues between North and South.[237] Whether Beijing or other potential donors would be open to attaching conditions to any financial contribution remains an open question.

Given structural flaws in Khartoum's economic model and the consequent effects on both national stability and North-South peace, it is critical that funds be harnessed to smoothing the fiscal transition, promoting productive sectors beyond oil and fostering greater economic decentralisation. If the money is not accompanied by political and structural reforms, the relationship between Khartoum and Juba may be destabilised again as soon as the money runs out. China and other potential donors must recognise the still interconnected nature of security between the Sudans and that coverage of the revenue gap and a deal on oil will not alone ensure stability and mutual economic viability.

The new Chinese special envoy, Zhong Jianhua, made his first visit to Sudan and South Sudan in mid-March to engage the respective leaderships on North-South issues as well as bilateral relations. In addition to contact with the AU, EU, and UK in February and early March, Zhong also reached out to the U.S. special envoy, Princeton Lyman. Like other partners, U.S. officials have warmly welcomed these signals, and the two envoys will soon meet to consider greater coordination of efforts.[238] Zhong's recent activity and signals may hint at more proactive engagement to come.

[234] Crisis Group interviews, Juba, February 2012.
[235] It remains unclear whether the approach has full backing in Khartoum; agreements were signed during the March talks on nationality and border demarcation but encountered some vocal opposition in Khartoum.
[236] U.S. Ambassador Dane Smith, who is primarily responsible for the Darfur file, travelled to the Arab world in March 2012 to consult partners.
[237] A deal on oil should also include Juba's agreement to maintain supply to the North for some time period, as well as Khartoum's commitment not to interfere with southern exports and to provide refined product to the South.
[238] Crisis Group telephone interview, March 2012.

VII. CONCLUSION

While the shutdown of the oil sector and consequent tensions could have disastrous consequences, the financial implications now unfolding for North and South could eventually alter the status quo at the negotiating table, long before an alternative pipeline can be constructed. China is in no way positioned to break the deadlock on its own, but its increased engagement, alongside that of other interested partners, could help secure a deal on oil and further issues critical to peaceful co-existence between the two Sudans.

Resolution of the North-South impasse and resuscitation of oil flows would undoubtedly influence the scope and character of the relationship that emerges. In the interim, the shutdown may temper the pace of otherwise expanding engagement between Beijing and Juba. Whether the political and economic ties already established will be robust enough to weather the current crisis remains to be seen, but both sides hope so. The diversity of Chinese interests and actors means the still developing relationship with Juba will not be determined, or coordinated, by government authorities in Beijing alone. These realities will continue to challenge China's attempt to strike the right balance within and between Sudan and South Sudan.

Juba/Beijing/Nairobi/Brussels, 4 April 2012

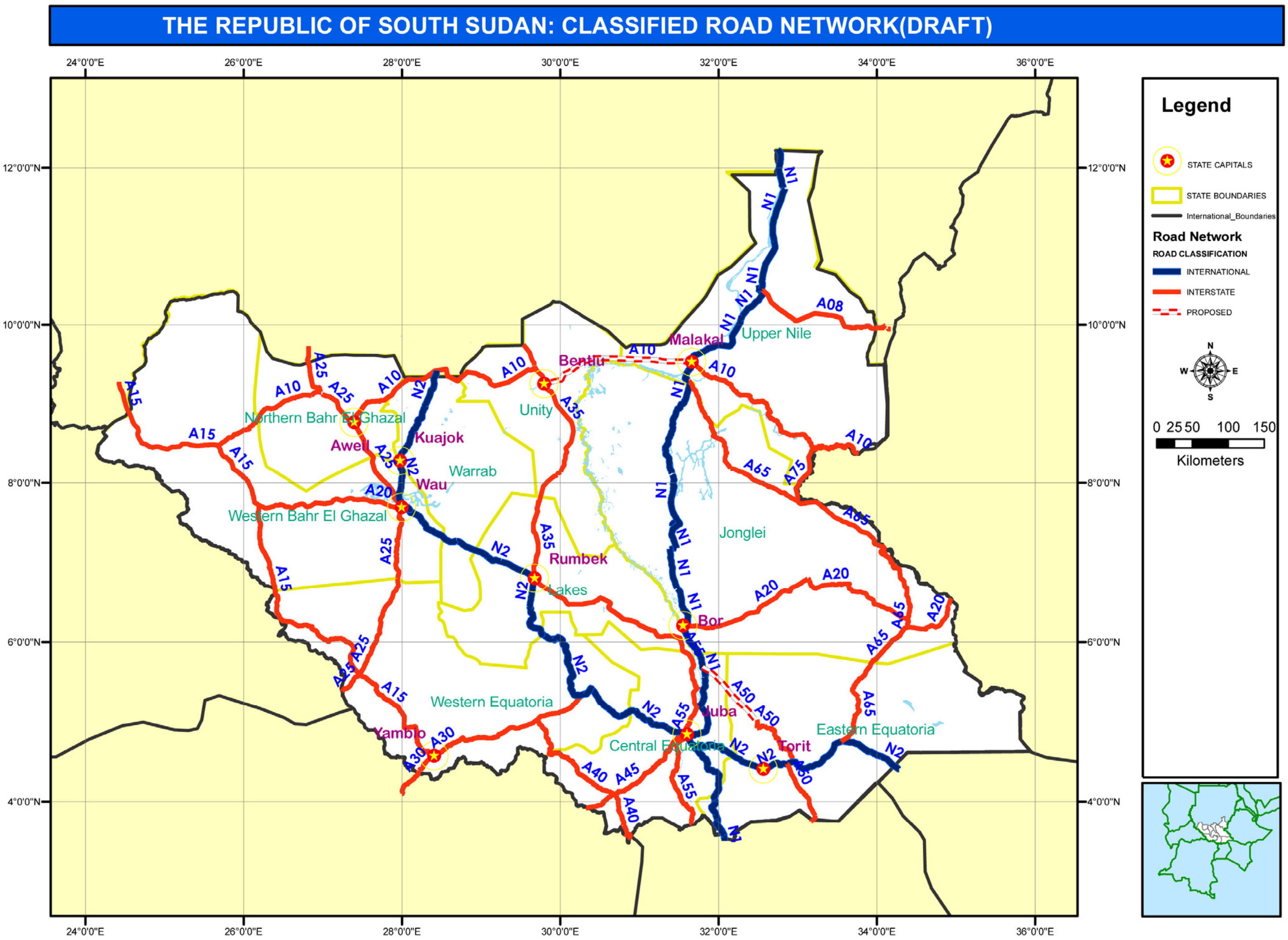
APPENDIX A

MAP OF THE REPUBLIC OF SOUTH SUDAN

Note: The map and boundaries represented are unofficial. They are meant for informational purposes only and do not claim to be definite.

APPENDIX B

MAP OF PROPOSED ROAD NETWORK, SOUTH SUDAN



This is an unofficial draft map of the proposed road network for South Sudan. It was produced for the GoRSS Ministry of Roads and Bridges through a USAID-funded capacity building project, and remains a working draft. Printed with permission from the copyright holder.

APPENDIX C

ABOUT THE INTERNATIONAL CRISIS GROUP

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Crisis Group's approach is grounded in field research. Teams of political analysts are located within or close by countries at risk of outbreak, escalation or recurrence of violent conflict. Based on information and assessments from the field, it produces analytical reports containing practical recommendations targeted at key international decision-takers. Crisis Group also publishes *CrisisWatch*, a twelve-page monthly bulletin, providing a succinct regular update on the state of play in all the most significant situations of conflict or potential conflict around the world.

Crisis Group's reports and briefing papers are distributed widely by email and made available simultaneously on the website, www.crisisgroup.org. Crisis Group works closely with governments and those who influence them, including the media, to highlight its crisis analyses and to generate support for its policy prescriptions.

The Crisis Group Board – which includes prominent figures from the fields of politics, diplomacy, business and the media – is directly involved in helping to bring the reports and recommendations to the attention of senior policy-makers around the world. Crisis Group is chaired by former U.S. Undersecretary of State and Ambassador Thomas Pickering. Its President and Chief Executive since July 2009 has been Louise Arbour, former UN High Commissioner for Human Rights and Chief Prosecutor for the International Criminal Tribunals for the former Yugoslavia and for Rwanda.

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April 2012

APPENDIX D

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APPENDIX E

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