

POWER POLITICS

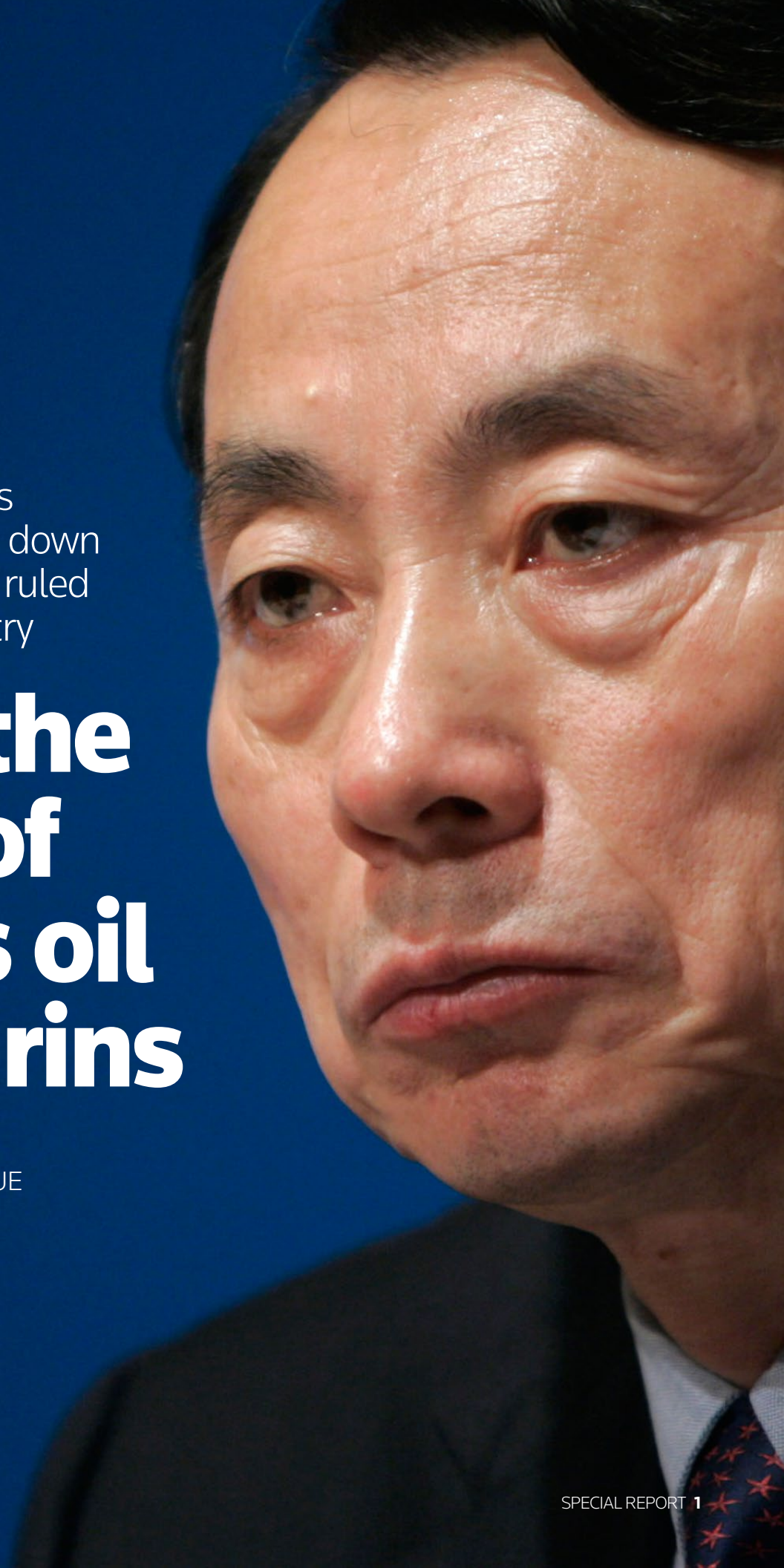
President Xi Jinping is systematically taking down a clique of rivals who ruled the petroleum industry

# Inside the purge of China's oil mandarins

BY CHARLIE ZHU, DAVID LAGUE  
AND BENJAMIN KANG LIM

FALLEN: Jiang Jiemin, former head of CNPC and PetroChina, was a lynchpin supporter of President Xi's rival, Zhou Yongkang.

REUTERS/PAUL YEUNG







ASCENDANT: President Xi, above, has targeted Zhou Yongkang in China's biggest corruption probe since 1949. **REUTERS/FENG LI/POOL**

BEIJING/HONG KONG, JULY 24

**O**il executive Jiang Jiemin rose to power in Communist China in time-honored fashion: by hitching his star to a mighty mentor.

In Jiang's case, that patron was another oil man, Zhou Yongkang, who went on to become the chief of China's internal security apparatus and one of the country's most powerful men.

Like Zhou before him, Jiang rose to the top of the country's biggest oil producer, China National Petroleum Corporation. In return, say people familiar with his career, Jiang helped Zhou build power by using the oil giant to dispense patronage. In March last year Jiang ascended even higher, when he was named to run the agency that

**“**The scale of the probe into CNPC is unprecedented.

**Qing Yi**

Beijing economist

oversees all of China's biggest state-owned companies.

Their relationship was on display ahead of the party's 18th congress in November 2012, when both attended a banquet for CNPC veterans of a 1980s drive to find oil in remote western China. In toasts and remarks, Jiang continually referred to Zhou as “the leader” and urged the oil men to “accept the leadership of the Party's central committee” and of Zhou himself, says an executive who was at the banquet. The flattery, the executive says, “was so obvious.”

Today, the retainer's loyalty to Zhou has backfired. In September, Jiang was sacked and arrested, a victim of a seismic power struggle as Chinese President Xi Jinping sets out to crush Zhou, the most senior leader targeted in a corruption probe since the Communist Party took power in 1949.

In a bid to isolate his rival, Xi is steadily taking down Zhou's extensive web of colleagues, political allies, relatives, staff and business associates of his family, according to people familiar with the investigation. Corruption investigators are swarming the CNPC group, where Zhou, 71, a geophysical engineer, built a vast network of friends and allies over the decades.

Jiang, 58, is the most senior executive to fall in an ongoing purge of current and former managers of the petroleum giant. He is

accused of using his position and CNPC's massive budget to help Zhou buy political favors and maintain his network of supporters across China, according to people with ties to the Chinese leadership.

The campaign against Zhou is roiling the entire Communist Party. A Reuters examination of the oil-industry component of the crackdown shows the extent of the purge, a drama that will have repercussions well beyond China.

"The scale of the probe into CNPC is unprecedented, but perhaps the severity of corruption at the company is also unprecedented," says Qing Yi, a Beijing-based independent economist.

CNPC is one of the world's largest companies, with global operations and 2013 revenue of \$432 billion. Its flagship publicly listed subsidiary, PetroChina, trades in Hong Kong, Shanghai and New York and is the world's fourth-biggest oil producer by market capitalization. Jiang ran both the parent and PetroChina from 2007 until last year, when he briefly headed the State-Owned Assets Supervision and Administration Commission (SASAC).

Interviews with senior CNPC officials, statements from the authorities and an analysis of the positions held by the arrested executives indicate that investigators are scrutinizing offshore and domestic spending, including oil service contracts, equipment supply deals and oil field acquisitions.

The investigation has already touched CNPC group operations in Canada, Indonesia, China and Turkmenistan, say people familiar with the proceedings. In addition to Jiang, the Chinese authorities have confirmed the arrests of CNPC vice president Wang Yongchun, PetroChina vice presidents Li Hualin and Ran Xinquan, and the listed unit's chief geologist, Wang Daofu.

Criminal prosecutors are now investigating Jiang and Wang Yongchun for bribery, the official Xinhua news agency reported July 14, without giving details.



BIG SPIGOT: A pump at a PetroChina station in Beijing. The CNPC unit is the world's No. 4 oil maker by market capitalization. **REUTERS/KIM KYUNG-HOON**

**\$432**  
billion

Annual revenue of the  
CNPC group

Source:CNPC

In China, the announcement of a criminal probe means charges are almost certain to follow. Acquittals are rare.

SASAC, the state-owned company regulator, said last year that Li, Ran and Wang Daofu were under investigation for "severe breaches of discipline." In China, this phrase is often a euphemism for corruption, but SASAC did not go into details.

Oil industry sources have told Reuters that another six senior CNPC group executives have been detained and are under investigation, but there have been no public announcements of these cases. Dozens of

other managers have been questioned as investigators methodically unravel Zhou's petroleum faction, according to senior officials at CNPC in Beijing.

The authorities have yet to reveal any specific evidence against Jiang or any of the other detained CNPC managers. CNPC and PetroChina did not respond to questions for comment on the investigation or arrests. The party hasn't made any public announcement about Zhou's fate.

As is routine in Chinese corruption cases, Jiang, Zhou and the other people named in this article as suspects couldn't be reached for comment, nor could their lawyers be identified.

While not dismissing the graft allegations, some Chinese say the purged officials appear, in part, to be victims of a brutal struggle within the Communist Party. "All this is not transparent, so people are suspecting that's the case," says Mao Yushi, an advocate of economic reform and honorary president of a private Beijing-based consultancy, Unirule Institute of Economics. "I

*Text continues on page 5*

# A political oilman: Jiang Jiemin

BY CHARLIE ZHU AND DAVID LAGUE  
HONG KONG, JULY 24

Throughout his career at China's biggest oil producer, Jiang Jiemin was careful to put politics before business, say colleagues who worked closely with the purged executive.

In strongly supporting government energy strategy, often at the expense of profitability, the former chief of China National Petroleum (CORP) was a vocal proponent of what he called national and social responsibility for state-owned enterprises, according to his speeches and public statements.

Jiang's former colleagues say the Shandong University-trained economist is a sharply different personality than some of the rough and tumble engineers and geologists at the top of CNPC. Jiang is a "reserved person," says a former executive who worked closely with him. "More of a politician than an oil man."

His polish set him apart from colleagues like current CNPC boss Zhou Jiping, a garrulous engineer widely known and liked in the global oil industry. Jiang's reserve, however, doesn't indicate a lack of ability.

Jiang started out in the 1970s as a junior worker in the Shengli oilfield, then China's second largest, in his native Shandong Province. "He is an extremely sharp guy," says one former colleague. "He's quick in grasping new subjects and when he speaks, he hits the right notes."

But Jiang's desire to please Beijing made him prone to overpromise and back expensive ventures, detractors inside the company say. Jiang was general manager and party secretary of CNPC when in May 2007 he became chairman of its flagship listed unit, PetroChina <0857.HK> <601857.SS> <PTR.N>. Almost immediately, he stunned the global oil industry and the party leadership with an announcement that

PetroChina had made a giant find in Bohai Bay off northeast China.

In a stock exchange filing, the company said it "believes the Jidong Nanpu Oilfield is a bulk, quality and efficient" field with reserves of more than 1 billion tonnes. Global oil major BP Plc <BP.L> estimates China has proven oil reserves of about 2.5 billion tonnes at the end of 2013. If confirmed, the Bohai discovery would have delivered a 40 percent boost to China's reserves at a time of accelerating reliance on imported oil.

China's then-premier, Wen Jiabao, told the official Xinhua news agency he was so excited upon hearing the news that he couldn't sleep. Investors were thrilled, too. PetroChina's shares in Hong Kong jumped 14 percent the day after the news.

Inside the company, some senior officials had doubts. Before the announcement, Jiang had told fellow managers that the Bohai find was a blockbuster. "But, we all understood Jidong is not a new field," said a senior Chinese oil industry official. "It was unlikely there could be such a big discovery there in light of geological conditions."

The company sank at least \$1 billion to explore the field and build a port and other facilities, according to public announcements. But over the following two years, excitement dwindled in company statements. There are no publicly available production figures for the field, and PetroChina rarely mentions Jidong Nanpu.

Jiang's judgment was also called into question when CNPC spent heavily to speed the construction of what he called "strategic corridors" for China's energy imports. These included long pipelines connecting China with Russia, Central Asia and Myanmar.

Over the objections of Chinese industrial planners, Jiang launched the \$1 billion, 2,520 kilometer (1,560 mile) Myanmar gas pipeline in 2010. It was completed in June 2013. As

analysts had predicted, it has been carrying only a fraction of its capacity, because the offshore Myanmar fields feeding the line were unable to supply enough gas.

Jiang also drove an investment boom when Beijing instructed state-run oil companies to secure more overseas oil supplies. Under him, PetroChina boosted its annual oil and gas production some 32 percent to 1.4 billion barrels over the seven years to 2013. Over the same period, the company expanded refinery output by almost a quarter.

Internal critics say Jiang drove this investment, sometimes without proper regard for cost or risk, because it would please his political masters. Given the priority the party leadership put on those strategic goals, to be sure, it isn't clear how much choice he had.

The expansion came at a price. Total liabilities jumped almost 200 percent from 348.3 billion yuan (\$56.13 billion) in 2008 to 1.07 trillion yuan at the end of 2013.

Return on equity fell to 10 per cent in 2012, down from a peak of 30 per cent in 2005. At HK\$10.80, PetroChina's Hong Kong listed shares are trading well below their 2007 peak of HK\$20. This is in contrast to the shares of other global oil majors, including Exxon Mobil <XOM.N>, which are hovering near record highs.

Since Jiang's arrest, the company has slashed capital spending. Even so, some senior executives say some of Jiang's strategic decisions - including the loss-making gas pipeline from Central Asia - could yield longer term benefits.

"We should not say all the previous expansion was wrong," says a senior PetroChina official involved in the company's offshore investments. "If we had not done it, it would be too late to do it now."

(\$1 = 6.2057 Chinese Yuan)



share the suspicion.”

Anxiety now grips the non-descript offices inside CNPC's steel-and-glass Beijing headquarters, according to staff working at the building. Managers are being regularly taken away for questioning, company officials say. Some prominent executives have returned to their desks after the interrogations, while others remain in custody. Senior staff told Reuters they expect more arrests.

To spearhead his crackdown, Xi has enlisted a close ally: Wang Qishan, a veteran official with a reputation as the Communist Party's top trouble-shooter and an implacable corruption fighter. Wang heads the Central Commission for Discipline Inspection, which as the party's internal watchdog division is the most powerful investigative body in China. On June 30, the commission said Jiang had been expelled from the party for corruption. The commission did not respond to requests for comment.

Xi is determined to bring down Zhou for allegedly plotting an audacious power grab ahead of the 18th Party Congress in November 2012, people familiar with the probe say. Zhou is accused of attempting to promote his supporters into the leadership so that he could rule from behind the scenes after he retired, they say. He has been under virtual house arrest in Beijing since late last year.

Zhou was a relentless networker over his decades at the top of Chinese industry and politics, oil industry veterans say, cultivating supporters throughout China. Jiang was one of his agents in building these connections. Some of this support for Zhou involved tapping the pork barrel.

At the helm of CNPC, Jiang recruited political allies for Zhou by approving proposals to build refineries in a number of provinces, a person with ties to the leadership told Reuters. “Local governments were grateful because the refineries helped boost their economies and created jobs,”



TROUBLED: Zhou in 2007, when he was China's chief of internal security. Authorities have arrested 300 relatives and allies. **REUTERS/JASON LEE**

\$14.5  
billion

Value of assets authorities say they've seized from Zhou clan and associates

Source: Reuters

the source said, without pinpointing specific deals. “Through Jiang Jiemin, Zhou Yongkang won over their loyalty.”

Under Jiang, one of CNPC's most controversial moves was a 2008 decision to build a \$6 billion refinery and petrochemical project at Pengzhou, near Chengdu, the capital of Sichuan Province. Zhou was party secretary in Sichuan between 1999 and 2002 and established a political stronghold in the southwestern province. Investigators

have made many arrests in Sichuan in the campaign against Zhou.

From the start, there were strong environmental protests against building a refinery in the earthquake-prone area. Some critics of the deal also questioned the wisdom of situating the complex so far inland, in an area far from ports and without major nearby oilfields. Most of China's major refineries are on the coast with easy access to imported crude.

Without mentioning Zhou, a CNPC official with knowledge of the project told Reuters that Jiang backed the plant because he wanted to please political leaders. “It doesn't make much sense to build the project there,” the CNPC official said. “Where do you source your crude oil?”

In its project proposals, CNPC said the Sichuan refinery would process oil from Russia, Kazakhstan and western China. Some industry analysts say southwest China has very little refining capacity, and the Pengzhou project fills that gap.

An earthquake devastated Sichuan in 2008. Undeterred, Zhou prodded local officials to beef up safety measures and press ahead with the refinery. "Build up Sichuan's heavy petrochemical industry," he urged on a 2010 visit to the province, according to reports in the state-run media. When the refinery started production this year, the National Development and Reform Commission, China's powerful economic planning agency, said it would boost the regional economy.

PetroChina, with a market capitalization of about \$225 billion, is China's dominant oil and gas producer, with global operations including oilfields, refineries, pipelines and petrochemical plants. It is a subsidiary of CNPC, and yet a power in its own right: PetroChina holds most of its parent's assets on its balance sheet.

While Jiang was at the helm of both companies, the group launched a spending bonanza, heeding a political command to secure access to more offshore oil as part of Beijing's campaign to boost energy security. PetroChina's annual capital expenditure almost doubled to about \$57 billion over the six years to 2012. In the five years to 2013, CNPC and PetroChina also spent \$25 billion on overseas assets. These outlays are now under the microscope.

CNPC vice-president Wang Yongchun was the first senior oil executive to fall, late last August, as part of a wider campaign to roll up Zhou Yongkang's network.

Days later, in early September, the probe into Jiang was made public. More than 300 of Zhou's relatives, allies and business associates have been arrested, detained or questioned, according to people briefed on the investigation. Authorities have seized assets worth at least 90 billion yuan (\$14.5 billion) from Zhou's family members and associates, they said.

Zhou's last public appearance was in Beijing on October 1. He has been under virtual house arrest since late last year, people briefed on the probe say.



POINT MAN: Wang Qishan, shown in 2009, is spearheading Xi's corruption crackdown.

REUTERS/TOBY MELVILLE

The probe has ensnared Chinese oil officials with ties to Indonesia, Iran, Kazakhstan and Canada.

Reuters

The purge then broadened:

- About the time Jiang was arrested, the former head of PetroChina's Indonesia operations, Wei Zhigang, was recalled from his post and is now under investigation, three Chinese oil industry sources told Reuters. Senior CNPC sources in Beijing say investigators may probe two oilfield acquisitions in Indonesia, where it appears the company overpaid for assets.

- In December, investigators detained CNPC's chief accountant, Wen Qingshan, two people with direct knowledge of the probe told Reuters. Wen was also chairman of PetroChina's Hong Kong-listed natural gas distribution arm, Kunlun Energy. In statements to the Hong Kong Stock

Exchange, the companies said Wen had resigned because of unspecified "personal matters."

- Early this year, Zhang Benquan, head of PetroChina's operations in Iran, was taken away for investigation, said two Chinese oil industry sources familiar with the situation.

- In May came the arrest of PetroChina's overseas operations chief, Bo Qiliang. Company sources told Reuters that investigators visited his Beijing home and took him away for questioning. In a statement to the Shanghai Stock Exchange on May 16, the company said Bo left his post due to an unspecified change in his role. Earlier, he was chief of PetroChina's operations in Kazakhstan.

- An oil industry official in Beijing confirmed a report this month in the financial news magazine Caixin that two other top oil men were under investigation: Li Zhiming, the head of CNPC and PetroChina operations in Canada, and Beijing-based Song Yiwu, deputy head of CNPC's overseas operations.

The investigation of Jiang also involves his alleged role in the use of CNPC funds to cover up a politically embarrassing tragedy.

Investigators have questioned Jiang over the transfer of CNPC funds to pay off the victims of a March 2012 car crash involving the son of Ling Jihua, a top aide to then-President Hu Jintao, three sources with ties to the Chinese leadership told Reuters.

Ling's son, Ling Gu, in his twenties, was killed while driving a Ferrari in Beijing. One of the two young women passengers was also killed and the other injured.

At the behest of Zhou Yongkang, Jiang arranged payments of millions of yuan to the dead woman's bereaved family and the surviving passenger in a bid to buy their silence, said the sources. All three sources, who are not political rivals of Zhou, said they were briefed by investigators or senior officials.

In helping cover up the crash, they said, Zhou wanted to gain influence over Ling.

When President Hu belatedly learned of the affair, he was disappointed and demoted Ling to head the United Front Work Department, a lower-level ministry. Ling and Hu could not be reached for comment. The United Front Work Department did not respond to requests for comment.

In expelling Jiang from the party, the Central Commission for Discipline Inspection didn't mention the Ling case or any specific findings against him. It said Jiang was guilty of taking advantage of his post to benefit others and extort huge bribes.

For a time after the car crash, Jiang's career appeared on track. At the 18th Party Congress in November 2012, Xi took over as party boss. Zhou retired. Jiang was elevated to the Communist Party's Central Committee, the elite, 200-odd member group which includes the seven members of the Politburo Standing Committee, the supreme decision making body headed by Xi.

If Jiang felt any disquiet about the crash probe, he showed no sign when he appeared that month at an assembly of bosses of state-owned firms in Beijing's Great Hall of the People. Dressed in a black suit and pink tie, he readily answered questions about CNPC's plans.

Xi, however, was gathering his forces against Zhou and the oil faction.

At the congress, Xi's fix-it man, Wang Qishan, was promoted to the all-powerful Politburo Standing Committee and named head of the party watchdog commission. That made Wang the second-most powerful leader in China behind president Xi, according to political insiders in Beijing. Wang immediately sharpened the watchdog's bite with extra investigators, publicly warning that no corrupt official was safe, no matter how senior.

The rolling purge has left PetroChina's board scrambling to keep markets informed



GLOBAL REACH: PetroChina's banner flies next to the national flag in Beijing last August. The probe has touched CNPC-PetroChina operations around the world. **REUTERS/KIM KYUNG-HOON**

as authorities ensnare top executives in the investigation.

"As soon as the news spread, the audit committee consulted hired lawyers in order to decide what appropriate course of action should be taken," says Franco Bernabe, the former head of communications giant Telecom Italia SpA, who served for some 10 years as an independent director of PetroChina until May. Bernabe declined to discuss specific allegations against the arrested executives.

Bernabe said management has tightened guidelines and procedures to limit the potential for graft. But some senior managers say the sheer size of the oil empire Zhou and Jiang built will make change very difficult. The CNPC-PetroChina group has dozens of subsidiaries and employs more than 1.6 million people.

One sign of the murk: Some senior PetroChina managers familiar with the investigation say they aren't even sure where in the sprawling conglomerate – parent CNPC, listed subsidiary PetroChina, or

the other units – each of the many alleged offenses is supposed to have taken place.

---

### FOR MORE INFORMATION

#### David Lague

david.lague@thomsonreuters.com

#### Charlie Zhu

charlie.zhu@thomsonreuters.com

#### Benjamin Kang Lim

benjamin.lim@thomsonreuters.com

#### Michael Williams, Global Enterprise Editor

michael.j.williams@thomsonreuters.com