Scotland's Economic Performance

Oil & Gas UK

Executive Summary
Oil & Gas UK is the leading trade association for the UK offshore oil and gas industry. It is a not-for-profit organisation representing almost 400-member organisations from independent oil companies to SME’s working in the supply chain. Our aim is to strengthen the long-term health of the offshore oil and gas industry in the United Kingdom by working closely with companies across the sector, throughout the UK, governments and all other stakeholders to address the issues that affect the industry.

Our members are based throughout the UK with a significant presence in the North East of Scotland and Shetland and so the economic wellbeing of these areas are closely linked to and impacted by that of the performance of the oil and gas industry generally.

Recent Performance:
Against the back drop of the most challenging of global downturns that this industry has ever experienced, industry has worked hard to improve its performance and competitiveness and this focus helped contribute to production on the UKCS increasing by 16 per cent – a significant achievement given that the basin had previously seen a consistent decline in production since 2000.

Companies have delivered unit operating cost (UOC) improvements greater than any other basin in the world since 2014 and the good performance is set to continue with UOC’s on target to fall below $15 per boe (barrel of oil equivalent), for the first time since 2010.

Although the maturity and complexity of the UK Continental Shelf (UKCS) means it remains a more expensive basin in which to operate, this is still a basin worth investing in with its significant hydrocarbon opportunities, established infrastructure, highly skilled workforce and globally competitive fiscal regime. So far, this year almost $8 billion worth of merger and acquisition activity has taken place on the UKCS within exploration and production companies alone. There have also been many deals within the service sector with new strategic partnerships forged as companies adopt new approaches and ways of working.

The UKCS has made significant progress across a range of key metrices. This is underpinned by new business models to maximise value from both late-life operations and new field start-ups.
• Moving towards incentive-based contracts rather than cost-plus
• Adopting asset-focused business structures rather than traditional function-led models.

The industry also established its own efficiency Task force (ETF), led by Oil & Gas UK, to act as a pan-industry catalyst for sustainable change and be a vehicle to communicate progress and develop good practice. Since then, supported by strong leadership from the ETF, companies themselves and the industry overall have transformed their efficiency, significantly reducing costs, improving production efficiency and realising real increases in capital efficiency. This fundamental change has put the industry’s future on a more secure footing.

However, the relative lack of new activity on the UKCS has had a significant impact on the domestic supply chain where revenues fell by 30 per cent on average between 2014 and 2016 and are expected to fall by a further 3 per cent in 2017. The fall in income has contributed to a significant reduction in the number of jobs supported by industry to an estimated 302,000 in 2017.

Challenges remain, and the industry is in urgent need of fresh capital investment from exploration and appraisal through to the development of new projects.

Future Growth:
Oil and gas has a vital role to play in the energy mix over the long term, from transport fuel to power generation, to space heating and industrial applications. As an affordable, reliable, lower-carbon fuel, natural gas helps achieve significant greenhouse gas (GHG) emissions reductions, replacing more carbon-intensive fuels. In the longer term, carbon capture and storage (CCS), could make a significant contribution toward reducing GHG emissions. Given the continued demand for oil and gas, the UKCS offers an affordable and secure source of energy.

Decommissioning:
Further opportunity lies in the nascent decommissioning market. Through to 2025, it is estimated that over £17 billion will be spent on decommissioning activity. Industry is working closely with the OGA, HM Treasury and BEIS to ensure that this activity is carried out as efficiently and safely as possible, providing scope for the supply chain to develop skills and expertise that can be exported to other basins.

Brexit:
Brexit brings challenges and opportunities that will be considered when investors are assessing opportunities on the UKCS. In the short-term, the weakening of Sterling in response to Brexit was positive for many oil and gas companies, particularly producers with a local cost base and supply chain companies with a propensity to export. However, in the long term, the wide range of potential approaches as to how the UK will leave the EU will have different implications for the oil and gas industry that the sector needs to understand and manage.
While the long-term impact of Brexit is uncertain, with analysis showing that the cost of trade for the whole industry could increase by as much as £500 million per annum if the UK reverts to World Trade Organisation rules, or could be reduced by around £100 million under optimal trade agreements.

- Potential investors also require clarity as to how the UK will respond to the macro-economic impact of Brexit.
- The UK Government must maintain a strong voice for our industry in Europe where indigenous oil and gas will continue to provide a vital part of the energy mix.
- Our industry needs frictionless access to the markets and people for our supply chain and protection of energy trading and the internal energy market, which have helped provide a secure, affordable energy to the UK for decades.

**Changes in the labour market:**
Looking ahead, the level of activity on the UKCS and the ability of UK-based businesses to win contracts overseas will largely determine the number of jobs supported by the sector. Direct jobs, more closely linked to operating expenditure, are likely to be more stable in the near-term. Indirect jobs, more closely linked to capital investment, have a less certain outlook as they are reliant on new project sanctions. Induced jobs are a by-product of spending across all areas of the business and the associated wealth being redistributed across the domestic economy.

- Latest estimates show that the oil and gas sector continues to support over 300,000 jobs in the UK through direct employment, indirect employment and jobs that are induced by the sector’s wider economic contribution.
- While hundreds of thousands of jobs across the UK are still supported by the sector, the latest estimate represents over 13,000 fewer jobs than were supported in 2016 and 160,000 fewer than the peak of over 460,000 jobs in 2014.
- Over the last 12 months, the pace of contraction has slowed significantly to just 4.2 per cent, compared with annual contractions of 19.4 per cent and 15.6 per cent in 2015 and 2016 respectively
- Supply chain companies continue to cope with low activity levels and a lack of future projects, the slowdown in employment contraction suggests that the largest reductions to the workforce may now be behind us.
- In 2017, changes appear to be more transformational, aimed at creating a sustainable workforce for the long-term.
However we continue to need key skills to deliver the industry of today and the future and therefore there is a need to undertake the following actions in relation to skills going forward:

- Increase the number of trained engineers
- Encourage greater take-up of science, technology engineering and mathematics (STEM) subjects, particularly among girls.
- Undertake a mapping of future skills demands that accounts for technical advances and recognise the importance of workforce engagement to the development and retention of skills.

In terms of seeing growth in our economy we are working within the fields of technology and innovation to:

- Anchor capability and expertise in the UK by delivering sustained investment in technology.
- Commit to further funding for the Oil and Gas Technology Centre to support commercialisation of new technology.
- Ensure the UK can act as a test-bed for the development and early deployment of new technology.

**Business Environment:** Alongside the national fiscal regime, we need to ensure that the business environment is a compelling one that attracts companies to invest sustainably in the UK.

We welcome the Barclay Review and the Minister’s recent announcement that the transitional rates relief scheme, which allows those in the hospitality businesses and offices to limit their rates bills to 12.5%, will be extended for a further year. We would ask that more certainty is provided regarding this scheme to allow for investor stability up until the recommendations of the Barclay Review are implemented.

In terms of the income tax and rates system, for many organisations, staff are recruited because of their high-value skills and this translates, typically to higher earnings. We would ask, that in considering the impact of the tax regime on the overall business outlook, it remains conducive to attracting, and retaining, skilled labour. Any differences in fiscal matters which will result in more bureaucracy cross border would also be detrimental to the overall business environment.