Companies are set to make £11.6 billion windfall on UK oil and gas in 2022. The UK government is missing this opportunity to fund an energy transition

May, 2022

Russia's war in Ukraine has spiked oil and gas prices as much of the world seeks to punish Russia, one of the world's largest oil and gas producers, for its senseless aggression. While consumers feel the pain of rising retail prices, the profits are largely made by oil and gas producers selling their product into overheated commodity markets. The average price of the UK North Sea based Brent crude oil benchmark rose from $86 per barrel (Bbl) in January to $117 in March. Gas prices have also spiked.

While some of the initial fears of extreme high prices appear to have eased, the war is clearly driving an expectation of inflated oil and gas prices for the foreseeable future. We used the Rystad Energy Ucube database, an energy industry data analytics service, to gauge the projected impact of the war on company profits from producing oil and gas in the UK in 2022. We found that while the average oil price in 2022 was expected to increase 58%, the projected profit from extracting UK oil and gas would rise on average by 111%. This provides a windfall for the UK oil and gas industry of an estimated £11.6 billion, primarily derived from the war's impact on oil and gas prices.

The projected free cash flow increase is derived from an increase in the projected average oil and gas price for 2022. The database is updated monthly based on market movements and company announcements among other things. In February, before Russia's invasion of Ukraine began, the average price for Brent Crude oil in 2022 was estimated at $70/bbl.

This aligned with the U.S. Energy Information Administration's December 2021 assessment.[1] At that time, projected increases in supply in 2022 were expected to lead to lower prices as supply and demand would become more balanced.[2]

On February 24, Russia began its invasion of Ukraine and oil prices spiked to $133 in early March before falling back. Rystad hiked its 2022 oil price to $88/bbl in the March update and $111/bbl in the April update. Our analysis is based on a comparison of the pre-war scenario of $70/bbl and Rystad's April basecase of $110/bbl. Free cash flow[3] estimates are based on Rystad's modeling of hundreds of individual oil and gas assets operating in the UK in 2022.

Top companies

The top ten companies by projected 2022 free cash flow are shown in Table 1. These ten companies are expected to enjoy over 66% of the total projected windfall, making an additional £7.7 billion of the expected 11.6 billion. Notable is the presence of Chinese state-owned CNOOC in the top ten. One of seven state-owned companies, including Russia's Gazprom, that could walk away with a collective £2.4 billion in free cash flow (see Table 2). Also notable is a 135% increase for Ineos Group, from £129 million to £303 million, which is majority owned by Britain's richest man Sir James Radcliffe.

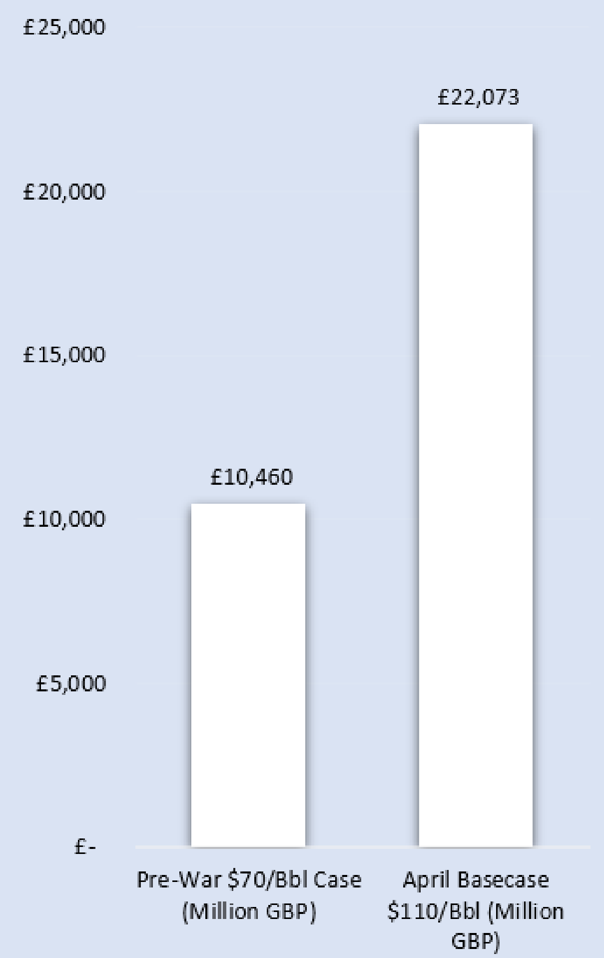

Figure 1: Projected 2022 Free Cash Flow from UK Oil and Gas Assets in Pre-War and April Basecases
Source: Rystad Energy Ucube (April 2022)

Rank	Company	Pre-War $70/Bbl Case (Million GBP)		April Basecase $110/Bbl (Million GBP)	
1	Harbour Energy plc	£	1,660	£	3,350
2	TotalEnergies	£	1,209	£	2,610
3	BP	£	1,035	£	1,964
4	NEO Energy	£	725	£	1,569
5	Shell	£	719	£	1,487
6	Delek Group	£	480	£	1,037
7	Spirit Energy	£	260	£	848
8	CNOOC	£	516	£	760
9	Eni	£	335	£	709
10	APA Corporation	£	341	£	647
	Total	**£**	**7,281**	**£**	**14,981**

Table 1: Top Ten Companies by Projected 2022 Upstream Free Cash Flow.
Source: Rystad Energy Ucube (April 2022)

Company	Pre-War $70/Bbl Case (Million GBP)		April Basecase $110/Bbl (Million GBP)	
CNOOC (China)	£	516	£	760
KNOC/Dana (South Korea)	£	237	£	530
Equinor (Norway)	£	233	£	439
NIOC (Iran)	£	138	£	331
Sinopec Group (China)	£	134	£	244
Gazprom (Russia)	£	33	£	80
Petronas (Malaysia)	£	1	£	2
Total	£	1,291	£	2,386

Table 2: State-Owned Companies
Source: Rystad Energy Ucube (April 2022)

A windfall tax could help alleviate energy poverty and fund the energy transition we need

UK oil and gas producers are benefiting from high global oil and gas prices caused by the war in Ukraine. A recent Wood McKenzie report concurs and reinforces the conclusion that profits from UK oil and gas production will soar in 2022.[4] A windfall tax on these profits would be reasonable and indicate the Government's commitment to fairness and leveling up. As Conservative Chancellor George Osborne observed when introducing a windfall tax in 2011: "oil companies are making unexpected profits on oil prices that are far higher than those they based their investment decisions on."

Under the current tax regime, oil and gas companies pay 40% total tax on the profits on extraction of oil and gas from the North Sea. This is the lowest government tax take in the world[5] for an offshore oil and gas regime.

The £11.6 billion increase in free cash flow, if fully requisitioned by the government, could relieve energy poverty in the UK and give a huge boost to insulation, energy efficiency, renewable energy and heat pumps that would help insure against future price shocks and reduce emissions.

For example, if five billion was used for supporting energy efficiency and clean energy development, the remaining £6.6 billion would provide the six million households experiencing fuel poverty £1,100 pounds each. This would still leave the oil and gas companies with the £10.5 billion in free cash flow they were in line to enjoy prior to Russia invading Ukraine and spiking prices (see Figure 1).

Oil and gas companies are unlikely to use free cash flow from oil and gas production to fund the transition to clean energy that is needed to help the UK both meet its climate goals and enhance energy security by reducing dependence on fossil fuels. In times of such unexpected profits, alongside the double-crises of the cost of living and the climate emergency, it is time for the government to step in and act, just as Osborne did in 2011. This time however, government intervention should both alleviate current pressures, with the £1,100 payment, and provide future-proofing, through household energy efficiency measures and support for an accelerated clean energy transition.

Methodology

We use the Rystad Energy Ucube database to query the production and economics of the upstream oil and gas industry. Upstream refers to the exploration and extraction of oil and gas. Upstream profit, or free cash flow, is revenue flowing from oil and gas projects to these companies after taxes and royalties, capital expenditure and operating expenditure. Debt service or other corporate costs, e.g. executive salaries, have not been extracted from these revenues. This free cash flow is therefore the profit derived at the project level from selling oil and gas produced before corporate expenses have been paid. Much of it could be used for executive bonuses, share buybacks, and investor dividends. Figures provided by the database are in US dollars.

We use a conversion factor of USD 1 = £0.765

This briefing was written by Lorne Stockman (Oil Change International),
and Charlie Kronick (Greenpeace UK),
published by Oil Change International
and Greenpeace UK.

For more information, contact:
Lorne Stockman
lorne@priceofoil.org
Charlie Kronick
charlie.kronick@greenpeace.org

Endnotes

[1] U.S. Energy Information Administration. December 2022. Short-Term Energy Outlook. https://www.eia.gov/outlooks/steo/archives/Dec21.pdf
[2] Brent had averaged $84.5 in November and $74.2 in December 2021.
[3] See Methodology.
[4] https://www.woodmac.com/news/opinion/-upstream-oil-and-gas-top-trends-and-wildcards-to-watch-in-2022-outlook/north-sea/
[5] https://www.rystadenergy.com/newsevents/news/press-releases/the-uk-offers-operators-best-profit-conditions-to-develop-big-offshore-fields-kuwait-canada-follow/