UK 2016 Budget: Rail, road and oil win out

Olivia Gagan

16/03/2016

The UK's 2016 budget was announced in Parliament on 16 March 2016 by Chancellor George Osborne, an annual event designed to set out the government's fiscal plans for the coming years. While energy policy was dominated by support measures for the oil and gas sector, rail and road projects led the infrastructure agenda.

Infrastructure

The budget placed a strong focus on the government's Northern Powerhouse scheme to improve connectivity in the north of the UK. The Budget effectively approved proposals already set forward by the National Infrastructure Commission (NIC), by giving its backing to a proposed High Speed 3 rail project between Leeds and Manchester, investing an extra £161 million ($226.9 million) to accelerate the redevelopment of the M62 to four lanes, and allocating £75 million to improve other road links across the North including the A66 and A69. The overall package is worth an estimated £300 million, Osborne said.

The budget also backed the NIC's London's Crossrail 2 proposal, a line which would run northeast to southwest across the capital. The government will provide £80 million to develop the project and will ask Transport for London to match this. The aim is to create a hybrid bill for the project during this parliament.

A trial run of 5G telecoms systems in the south west is also being planned, Osborne said.

Perhaps tellingly, these are projects without clear-cut budgets and at early stages of development - the High Speed 3 concept was officially backed by the NIC only yesterday.

Law firm Clyde & Co partner Robert Meakin suggested the budget focused on projects which to date have yet to be bogged down in public perception and planning issues. There was no mention of the UK's ongoing airport capacity issues, for example.

"All of the NIC's headline projects – Crossrail 2, HS3, M62 – have easier sells than the current troubled trinity of HS2, Hinkley and Heathrow," he said. KPMG's head of transport James Stamp, head of transport at KPMG agreed. He said that the rail announcements were "encouraging" but that the Chancellor "continues to prevaricate on the very real long-term problem of creating new airport capacity."

Transport and infrastructure partner at Pinsent Masons, Jon Hart, said the announcements will likely be greeted "with a reasonable degree of cynicism. This is perhaps a consequence of the previous trend of announcing, re-announcing and re-re-announcing the same capital expenditure between separate DfT policy paper announcements, autumn statements and treasury budgets.

"Make no mistake, the sums being (re)announced are an important allocation of seed money. That said, for the NIC's recommendations to be satisfied, the vested interests in the Chancellor's northern projects will need to be carefully coordinated – and soon – to avoid these sums not delivering their full potential."

Energy

Energy, meanwhile, appeared to receive less attention from the Treasury. While Chancellor George Osborne's references to energy policy were relatively few in his statement to parliament, the full budget document did set out further energy measures, which focused on oil and gas and emerging storage and nuclear technologies. The one bright spot for renewables: a budget was set for the next round of contract for difference (CfD) auctions.

Networks and storage

The government said it will allocate at least £50 million over five years for innovation in energy storage, demand-side response and other smart technologies. Ofgem will consult later this year on the future of its £100 million grid Network Innovation Competition.

The budget also mentioned an increased focus on inter-connector technologies, such as the UK-Belgium Nemo link.

Renewables

The budget said government will auction contracts for difference of up to £730 million during this parliament for up to 4GW of offshore wind and other "less established" renewables. The first auction, likely to be this autumn, will be for £290 million of contracts.

Support for offshore wind will be capped initially at £105/MWh, falling to £85/MWh for projects commissioning by 2026. This pricing places offshore wind on a par with nuclear technology – the Hinkley Point C nuclear project, for example, has signed a £92.50 per MWh support contract.

Mentions of climate change were scant, but the document outlined a plan to abolish the "bureaucratic and burdensome" UK carbon reduction commitment scheme and replace it with an increase in the country's climate change levy from 2019.

Nuclear

While the budget failed to make any mention of the UK's fraught, flagship power project Hinkley, it did mention the launch of the first stage of the UK's small modular nuclear reactor (SMR) competition, which will generate a list of SMR developers. The government will allocate at least £30 million for a research and development programme for the technology.

Oil & gas

The government will effectively abolish its petroleum revenue tax, by permanently reducing the rate from 35% to 0%, with the change backdated to 1 January 2016, it was confirmed. The industry's 'supplementary charge' levy is to be cut from 20% to 10%. This change will also take effect from 1 January 2016.

The government is willing to consider proposals for using the UK guarantees scheme for new investment in oil and gas assets, it said.

Developer Ecotricity founder Dale Vince said: "The budget is remarkable not so much for what's in it, but for what's not; the chancellor forgot to mention a little thing called climate change… What is this budget, and this Chancellor, doing on this front? Very little it seems."

Antony Skinner, renewables partner at law firm Ashurst said: "This is good news to an extent but the level of support being offered to offshore wind is being squeezed. The initial cap of £105 per MWh, later falling to £85 per MWh, is significantly lower than the administrative strike price of £140 per MWh originally set, or the strike prices of around £120 and £114 achieved in the first CfD allocation round. Also, it's not clear whether any established technologies will be offered support at all."

Richard Cockburn, energy partner at Bond Dickinson said the tax reductions will help significantly to improve the economics of North Sea projects. "The effective abolition of Petroleum Revenue Tax has long been called for by the industry," he said, and added "the reduction of the supplementary charge may allow operators to take a second look at projects which, until now, were looking uneconomic."