JERSEY'S FISCAL POLICY PANEL

Annual Report

September 2024

Fiscal Policy Panel Annual Report 2024

This is the seventeenth annual report of the Fiscal Policy Panel (FPP). The current members of the Panel are:

Sir Jon Cunliffe (Chair, appointed 2024),

Professor Francis Breedon (appointed 2016),

Professor Richard Davies (appointed 2018).

Amanda Rowlatt CBE (appointed 2024).

The Panel was placed on a statutory basis in 2014. The FPP's statutory role was reiterated in the Public Finances Law (2019), which requires the Panel to comment on Jersey's fiscal policy with reference to:

a. the strength of the economy in Jersey;
b. the outlook for the economy in Jersey;
c. the outlook for world economies and financial markets;
d. the economic cycle in Jersey;
e. the medium-term and long-term sustainability of the States' finances and the States' financial assets and liabilities; and
f. the advisability of transfers to or from the Strategic Reserve Fund and Stabilisation Fund.

The Panel's work is guided by five key principles, set out in the first Annual Report produced in 2008. These are:

1. Economic stability is at the heart of sustainable prosperity;
2. Fiscal policy needs to be focused on the medium term;
3. Policy should aim to be predictable, with flexibility to adapt to economic conditions to assist in creating a more stable economic environment;
4. Supply in the economy is as important as demand; and
5. Low inflation is fundamental to the competitiveness of the economy.

In making its recommendations, the Panel is guided by its understanding of the preferences of Islanders who want government to be prudent and create the conditions for economic growth while respecting the Island's cultural heritage, maintaining the competitiveness of the economy and keeping inflation low.

Budget 2025 was lodged earlier than usual. As a consequence the timing of this report has been brought forward. This has meant that the Panel has had

to work with out-of-date GVA data and has therefore placed greater reliance on other data, including the Business Tendency Survey (BTS). The Panel proposes to publish an Economic Outlook report in early 2025 which will include 2023 GVA data.

In preparing its reports the Panel draws on discussions with stakeholders and is grateful for the invaluable support provided by the staff of the Government of Jersey, in particular the Economics Unit and Treasury and Exchequer. More information about the Panel, including previous reports, can be found at [www.gov.je/FiscalPolicyPanel.](http://www.gov.je/FiscalPolicyPanel)

Foreword

Jersey is a high-income country that has recently experienced unusually strong economic growth. It is experiencing strong growth in tax revenues, driven almost entirely by profits in the financial sector. Higher banking revenues and profits are being generated primarily by external factors that are not within the control or influence of the Government of Jersey and thus cannot be relied on. The island is also facing several macroeconomic challenges including low productivity and an ageing population.

Jersey benefits from a strong financial services sector, which is responsible for nearly half of economic output directly and much more indirectly via spend by financial services firms and staff in the local economy. Jersey's economy and the quality of life enjoyed by islanders is highly dependent on the continued strength of its financial services sector.

This dependence on the financial services sector, however, is also a source of risk as many of the factors that determine financial sector revenues and profits are outside Jersey's control. At the same time, without its own currency and with relatively low tax and benefit regimes, Jersey lacks most of the key policy levers used in larger economies to smooth economic volatility and respond to major shocks. To address this, Jersey has established reserve funds such as the Strategic Reserve and the Stabilisation Fund. These funds – their value and liquidity – are very important for Jersey's economic stability.

The earlier lodging of the Budget has enabled this year's Annual Report to have been brought forward. However, this also means that it has been produced without the benefit of 2023 GVA data. The absence of more frequent GVA data makes assessing how Jersey's economy is performing difficult. Nonetheless, the data and information available to the Panel suggests that the banking sector saw strong growth in 2023, but that the rest of the economy may have seen little or no growth. Such a dependence on growth in one sector of the economy across sectors presents risks that needs careful management.

Jersey's economy typically operates at full employment with a reliance on migrant workers to fill additional and seasonal roles. These, often seasonal, workers are increasingly being recruited from further afield which requires forward planning and longer timelines. This may be making it harder for businesses to match employment with actual business activity. Coupled with employment restrictions that apply to these workers, this is creating rigidities in the labour market which in turn may be negatively affect the functioning of Jersey's economy.

Inflation is falling, but there are emerging signs that domestically generated inflation may be becoming more entrenched. This is challenging for an economy without nationally focussed monetary policy. A Budget that increases the growth in day-to-day spending (an expansionary fiscal policy) is likely to push up inflation and the demand for imports, rather than just improving incomes in the country.

The Panel has assessed the Budget in line with the underlying principles that inform the Panel's role. The Panel recognises that, in spite of stronger revenues, the Government of Jersey faces difficult choices and needs to balance pressure on day-to-day spending, particularly after the pandemic and cost-of-living shocks, against investing in the future and restoring the island's reserves to the levels necessary to safeguard the island's resilience to future shocks. The Panel's overall assessment is that in making these and future fiscal choices, and in the light of stronger revenues, greater emphasis should be given to the medium term and on ensuring the resilience of the island's economy to cyclical and structural shocks.

Executive Summary

Economic Outlook

- **The outlook for global growth in the near term remains stable but below pre-pandemic levels**. Global inflation has fallen considerably from its 2022 peak, but remains above target in many economies and the risk of persistent inflation remains amongst a background of escalating geopolitical tensions and increased uncertainty.
- **Jersey's economy is likely to have benefited from strong economic growth in 2023**. As in 2022 this growth is likely to have been driven by strong profit growth in banking, well above the historical average. By contrast, economic growth in the rest of the economy is likely to have been weak. With banking profits forecast to grow at a much slower rate from 2024, the outlook for economic growth is comparatively weaker.
- **The introduction of the OECD Pillar Two framework will mean a change in the tax regime.** This will directly affect Jersey's financial sector and, by extension, the island's economy. All else equal, tax receipts are expected to increase in the short-term but the change inevitably creates some uncertainty about the future.
- **Jersey's economy typically operates at full employment**, relying on migrant and seasonal workers to fill new and additional jobs. The number of jobs filled rose by 1.1% in 2023, whilst the number of people registered as actively seeking work (a measure of unemployment) remains low (below 700 people). Further, there are indications that the labour market may not be operating as flexibly as it might.
- **Headline inflation has fallen over the last year to 5%.** It is forecast to fall further as interest rates are expected to be reduced. However, the recent uptick in underlying inflation could be indicative of domestically generated inflationary pressures.
- **Housing market activity has slowed**. Turnover fell by 43% and prices fell by 3% in 2023. The fall in house prices has been more than offset by higher mortgage costs, as such housing affordability has not materially changed. The high cost of housing continues to be a potential drag on productivity.
- **Real earnings grew in 2024**. However, between 2020 and 2024 real earnings decreased by 3.3%. The fall in real earnings is largely because inflation has been high, but also reflects low productivity. Looking ahead, productivity will need to increase so the economy can support an ageing population without a reduction in living standards.

Fiscal Outlook (Public finances)

- **Public expenditure is growing**. The growth is in day-to-day spend rather than investment into the economy's productive capacity. Despite an increase in an already strong tax revenue forecast, there will be an operating deficit in 2025 and 2026, with only a small surplus in 2027. The increase in public spending in an economy with little spare capacity, risks pushing up inflation and pulling in more imports, significantly reducing any beneficial impact on real incomes.
- **Capital.** Budget 2025 includes plans to deliver Phase 1 of the New Hospital Facility. This will be a major capital investment of up to £710 million and care will be needed, given the risk of inflation, particularly as departmental capital budgets have previously been underspent because of capacity and/or capability constraints. The Panel welcomes the planning of these budgets at more realistic levels, but would have preferred that the "saving" was used to strengthen the Stabilisation Fund or Strategic Reserve rather than be spent on additional day-to-day spend (also known as "current" spending).
- **The central tax revenue forecast has increased** but none of this additional tax revenue has been allocated to improving the resilience of the economy through replenishment of the Stabilisation Fund or the Strategic Reserve, as recommended in previous Panel reports. The Panel commends the approach to forecasting Pillar Two revenues and is pleased to note that the Budget proposes to invest a portion of base case Pillar Two tax receipts into the Stabilisation Fund.
- **The Strategic Reserve is significantly lower than the 30-60% of GVA range that the FPP has recommended.** The Panel welcomes the commitment to invest PYB revenues in the Strategic Reserve but notes that the Strategic Reserve will only be equal to 17% of GVA in 2028 and that the cash value will be lower still.
- **The Stabilisation Fund is effectively exhausted.** The balance remains below £1 million and the Stabilisation Fund will be unable to deliver countercyclical fiscal policy via funding injections in times of economic downturn. The Panel welcomes the decision to allocate £41.6 million (over Budget 25-28) of the expected base case receipts from the Pillar Two income forecast to rebuilding the Fund. However, the Panel calculates that the recent period of strong and above trend economic growth means that had the Government adopted an appropriate counter-cyclical fiscal stance, a minimum of £50-80 million would have been invested in the Stabilisation Fund since 2021. The Panel notes that the opportunity for using the stronger tax revenues to

replenish the Stabilisation Fund, as recommended in its previous report, has not been taken.

- **Healthcare costs are rising.** Jersey spends a high proportion of its budget on health, more so than in OECD countries. 76% of the Budget's total expenditure growth for 2025 – 2028 is being spent in the Health and Community Services department. This rate of growth in healthcare spending is not sustainable given that income growth is forecast to fall back to much more moderate levels. Health demands are likely to rise faster than incomes which will mean difficult choices in the medium term between funding for healthcare versus funding for other important areas of the economy.
- **The value of Jersey's net assets is falling.** In 2019, net-asset-value as a percentage of GDP was 152%. This figure will fall to 111% in 2028.

Summary of recommendations

1. **Fiscal Strategy and Spending.** The Panel recognises there are pressures for higher current spending in Jersey, particularly following the pandemic and the cost-of-living crisis. The Government faces difficult choices in balancing these current spending pressures against investment in the island's productive capacity as well as addressing the depletion of the island's reserves. The Budget includes some welcome measures to rebuild the reserves in the longer term. Nonetheless, the Panel is concerned with the prioritisation given to current (or day-to-day) expenditure growth, rather than rebuilding the reserves and using strong tax revenue to preserve resources for future investment. In line with the principles which guide its work, the Panel believes that fiscal decisions need to give greater consideration to medium term challenges, ensuring the Island's economy is resilient to cyclical and structural shocks in an increasingly turbulent global economy.

2. **The Strategic Reserve** is significantly below the level the Panel believes is necessary to provide economic resilience and to protect Islanders from the impact of major crises. The Panel welcomes the decision to invest the proceeds from Prior Year Balance taxation debts into the Strategic Reserve. This will provide the Strategic Reserve with much needed support in the long run, but in the short and medium term the Strategic Reserve will remain below recommended levels making Jersey's economy vulnerable if a crisis was to occur. Further action to increase this reserve should be taken as a matter of urgency.

3. **The Stabilisation Fund** is effectively exhausted and cannot fulfil its purpose by delivering cyclical Fiscal policy to support Jersey's economy in the case of an economic downturn. The Panel's assessment is that the recent period of strong and above trend growth experienced since 2021 should have resulted in a minimum of £50-£80 million (and more likely £60m-£250 million) investment into the Stabilisation Fund. The Panel is pleased to note the intentions to invest a proportion (£41.6 million) of the base case Pillar Two tax revenues into the Stabilisation Fund and to invest surpluses of up to £25 million, from the Consolidated Fund, into the Stabilisation Fund in 2025. The Panel recommends that further, immediate action be taken to improve the balance of the Stabilisation Fund. This could take the form of a commitment investing a proportion of cyclical tax revenues into the Stabilisation Fund as well as a commitment to invest a proportion of upside/additional Pillar Two revenues.

4. **Pillar Two**. The implementation of Pillar Two will mean a change in the tax regime primarily affecting financial services. The Panel welcomes the Government's prudent approach to forecasting Pillar Two revenues. These future tax revenues create an opportunity for the Government to restore States Reserves to the levels needed to protect current and future generations of Islanders from economic shocks and instability. Investing Pillar Two income in reserves will generate future investment returns which could in turn be used to fund investment into increasing Jersey's productive capacity, crucial for long-term economic growth. Such a prudent approach in the short term is recommended considering the medium-term risks around the changing global tax regime.

5. **Healthcare expenditure and related funds.** Budget 2025 has allocated £124 million, in expenditure growth over 4 years, to healthcare. Spend on Health and Community Services will equate to 27% of total Government expenditure; this is high by OECD standards. The level of healthcare spend is a societal and political choice, but the rate of growth in healthcare spend is not sustainable given that income growth will fall back to much more moderate levels. The Panel notes that health demands can be expected to rise faster than incomes creating pressures for further spend. Managing this pressure will have consequences as it limits spending on other areas of the economy too, such as public services and investment into productive capacity for economic growth.

6. **Inflation and overheating**. Headline RPI inflation is falling, but there are signs that inflationary pressures may be building on Island (shown by an increase in RPIX last quarter) putting further pressure on the cost of living faced by islanders. The Panel is concerned that the proposed expenditure growth, when there is little spare capacity in the Island, can be expected to generate additional inflation or force demand offshore, outside of Jersey's economy.

Previous recommendations

The following table evaluates to what extent Government has implemented the previous FPP report's 2023 recommendations in the Budget 2025-2028:

Recommendation	Assessment
1. Government's long-run goals Meeting long-run economic challenges are vital for the future stability of Jersey's economy. **Action needs to be taken**	• Spending to meet short-run needs (day to day/current expenditure) has been prioritised over addressing long run challenges through investment in productive capacity or investment in the Reserves. • The capital programme has been reduced to a more realistic level, but the monies have been reallocated for day-to-day spend rather than saved to improve resilience or to fund future investments into Jersey's infrastructure and productive capacity.
2. Reserves The FPP recommended that urgent action be taken to replenish Government reserves **Some action has been taken, but this has not sufficiently improved the value of the reserves in the short to medium term**	• The Panel welcomes the decision to invest the PYB revenues in the Strategic Reserve. Nonetheless the Strategic Reserve's position is set to deteriorate further over the budget period, falling to only 17% of GVA by 2028. • The Stabilisation Fund has not been replenished despite stronger tax revenues from above trend economic growth. • The Panel welcomes the proposal in the Budget to invest some of the base case Pillar Two tax revenues into the Stabilisation Fund. It also notes the proposal that a proportion of any additional Pillar Two tax revenues (above the base forecast) should be invested into the Stabilisation Fund. The Panel welcomes this, but recommends a formal commitment is made.

3. Housing The FPP noted that housing affordability is likely to be a drag on productivity and a risk to economic growth	• Housing affordability has not materially changed, and the high cost of housing continues to be a potential drag on productivity.
4. Fiscal Strategy and Spending The FPP recommended the strong growth in Government income be used to rebuild reserves and not fund current expenditure **The operating balance has deteriorated and whilst the balances of the Stabilisation Fund and Strategic Reserve will improve slightly, both are insufficient.**	• The strong growth in government revenues is outstripped by faster growth in expenditure. The operating balance has deteriorated. • The balances of the States Reserves are deteriorating. Whilst some action has been taken, neither the Strategic Reserve nor the Stabilisation Fund have the balances required to fulfil their purpose. This places Jersey's economy at greater risk should a crisis or economic instability arise.
5. Inflation The FPP warned that the Government's fiscal stance was adding additional demand into an economy operating at/above capacity. This risks higher inflation. **No action has been taken and Jersey's position has worsened**	• Additional government expenditure risks inflation increasing or not falling as fast it would otherwise. It might also force demand offshore. Either (and both) would reduce the beneficial effect on real incomes that Government spending can have.

6. Health-related funds

The FPP considered the sustainability of the States health-related funds.

No action has been taken and Jersey's position has worsened

- The rising costs of healthcare is rapidly eroding the Health Insurance Fund and straining the growth of the Long-Term Care Fund.
- Under the current Budget proposal, £2 million in additional annual withdrawals will be made from the Health Insurance Fund – this reserve is now expected to be fully exhausted by 2030.

The Economic Outlook

1.1 International outlook

1.1.1 World Growth

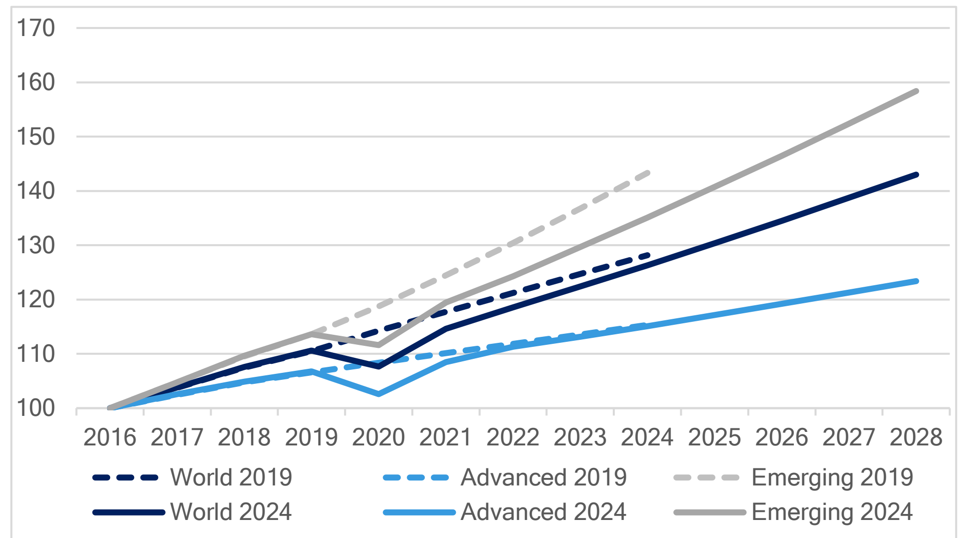
Global economic growth is currently slower than the pre-pandemic average, with continuing risks to inflation. Whilst growth in advanced economies is now in line with the pre-pandemic projected path, emerging market and developing economies remain below pre-pandemic growth projections (**Figure 1.1**).

Figure 1.1

Real GDP, 2016 - 2028, 2016 = 100

Index of real GDP, October 2019 (dotted line) and April 2024 (solid line) estimates/forecasts

Sources: International Monetary Fund World Economic Outlook



In the International Monetary Fund's (IMF) July 2024 forecast update, "*The Global Economy in a Sticky Spot*", 2024 global growth forecast is unchanged at 3.2%. The IMF highlight upside risks to inflation and higher-for-longer interest rates against a background of escalating trade tensions and increased uncertainty, recommending that fiscal and monetary policies be sequenced to achieve price stability and to replenish depleted buffers.

Figure 1.2 shows the forecasts for the rate of growth of the global economy (in terms of Gross Domestic Product (GDP)) from 2024 to 2028. By 2028, global growth is forecast at 3.1%, which is below the 2000-2019 average growth rate of 3.8%. The weaker outlook compared to the previous two decades reflects a range of factors, including higher interest rates, longer-term effects from Covid and Russia's invasion of Ukraine, low productivity growth, and increasing geoeconomic fragmentation.

The latest IMF update indicates that differences in growth rates among advanced economies are narrowing. Whilst growth in the US economy surpassed expectations throughout 2023, it is now showing signs of cooling. In contrast, growth in the Euro area is beginning to increase after being relatively flat in 2023.

India and China are forecast to account for almost half of global growth. Despite continued weakness in China's property sector creating uncertainty over the outlook, the IMF has revised its growth forecasts upwards for China following a rebound in domestic consumption in the first quarter of 2024.

Overall, risks to the global economic outlook remain balanced but near-term inflation risks have become more prominent. Inflation has fallen considerably from its 2022 peak, but escalating trade tensions risk creating inflationary pressures and the risk of interest rates remaining higher for longer, with adverse impacts on growth.

Fiscal resources in many countries remain depleted following government support to mitigate recent crises (e.g. Covid), leaving public finances in a more vulnerable position to respond to future shocks

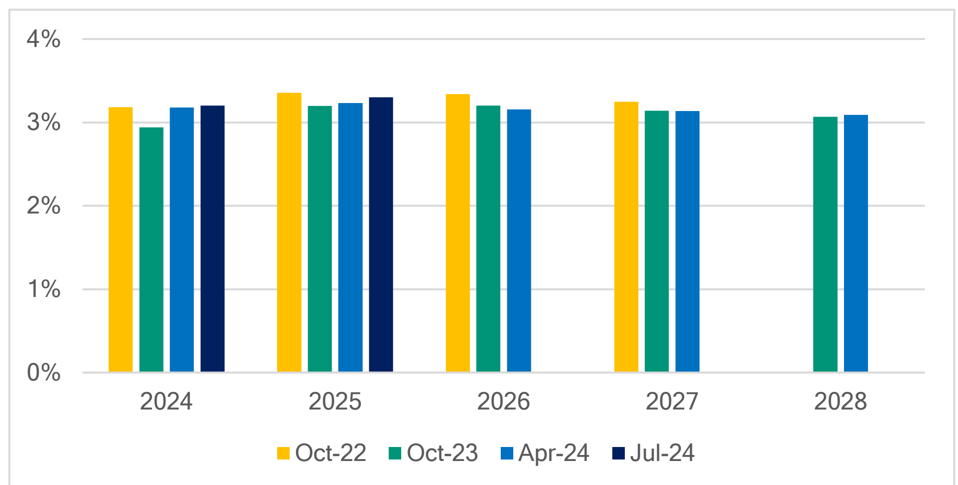
Figure 1.2

Forecasts of global real GDP growth, 2024 - 2028

Forecasts of global real GDP growth, percentage (%), 2024 - 2028, October 2022, October 2023 and April 2024 projections

Note: The July 2024 projections only cover 2024 and 2025.

Sources: International Monetary Fund World Economic Outlook



1.1.2 UK Growth

Following weak growth in 2023 (real GDP increased by 0.1%), UK economic growth has picked up in 2024. High interest rates continue to weigh on consumption, but recent growth in real household incomes and falling interest rates are expected to support future consumption growth.

The latest IMF forecast has revised up its growth projections for the UK to 0.7% in 2024, slower than the 1.7% rate of growth forecast for advanced economies. By contrast, the Bank of England has forecast UK GDP to grow at a faster rate of 1.25% in 2024. Slower UK growth relative to other economies is of particular significance for Jersey as the UK is our major trading partner.

The sterling trade-weighted index (**Figure 1.3**) appreciated by 3% from January to July 2024, putting downward pressure on import price inflation. However, following the Bank of England decision to cut interest rates in

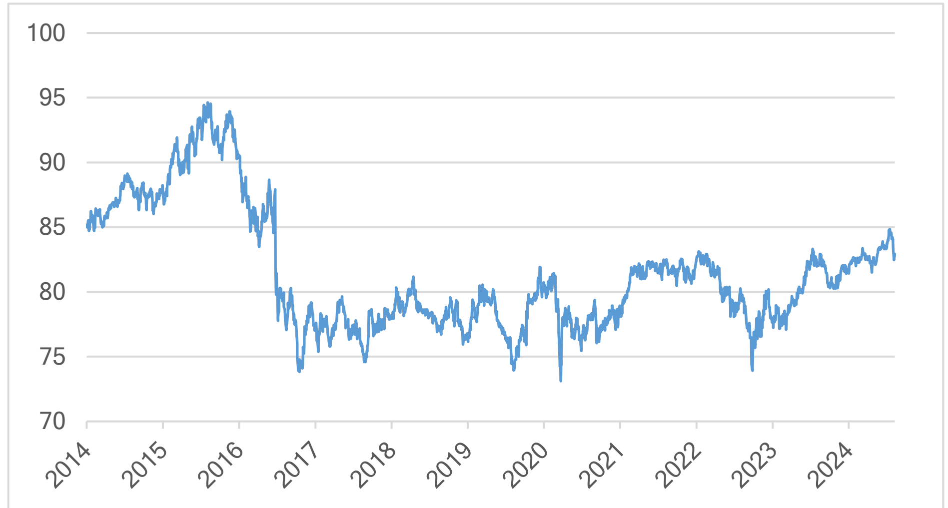
August 2024, sterling depreciated slightly, with markets expecting a further interest rate in 2024.

Figure 1.3

Sterling's trade-weighted index, Jan 2014 - Aug 2024, Jan 2005 = 100

Effective exchange rate index, Sterling (Jan 2005 =100), Jan 2014 - 9 Aug 2024.

Sources: Bank of England



Falling oil and gas prices (**Figure 1.4**), have contributed to falling UK inflation. In the twelve months to July 2024, the price of gas rose by 12%, whilst the price of crude oil increased by 4%. Geopolitical tensions create uncertainty over the outlook for energy prices.

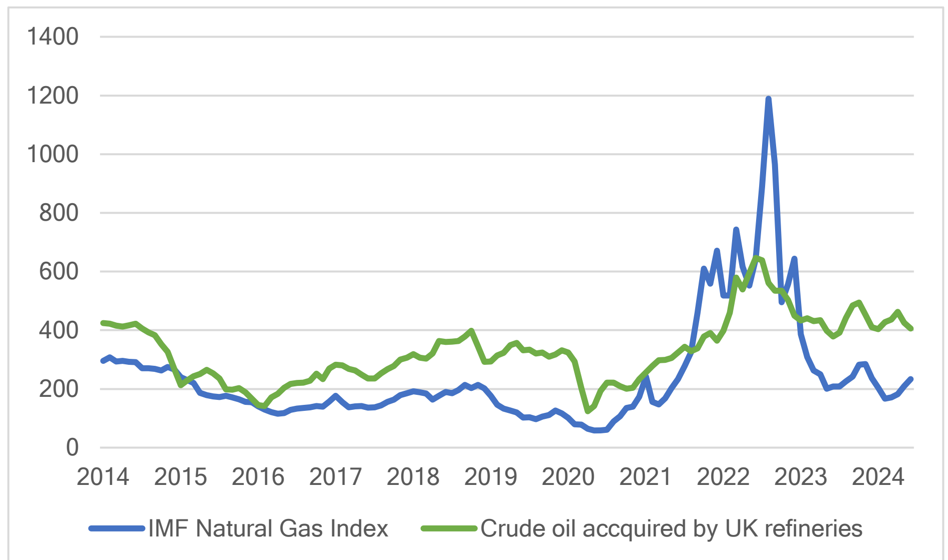
Figure 1.4

Crude Oil and Natural Gas Prices 2014-2024

The price of crude oil acquired by UK refineries measured monthly (Jan 2000 = 100)

IMF Commodity Prices index for natural gas (Jan 2000 = 100)

Sources: DESNZ, IMF



1.1.3 UK Inflation and close trading partners inflation

Since its peak in 2022, inflation has been falling in the UK and in other advanced economies, driven by factors such as falling energy and food prices and tightening monetary policy. The UK's key measure for inflation, CPI, was at 2.2% in August 2024, broadly in line with the Bank of England's 2% target. UK inflation is forecast to rise slightly to the end of 2024, before falling back to

2% by 2026. In other advanced economies, the pace of disinflation is slowing, with both the US and the Eurozone continuing to experience above target inflation.

1.1.4 Interest Rates

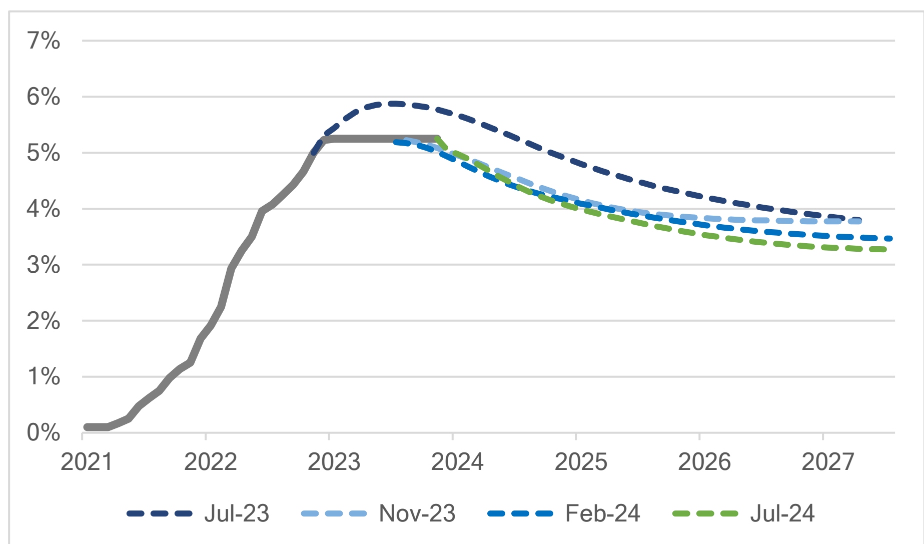
The Bank of England base rate is now at 5%, following a cut from 5.25% in August 2024 - the first cut to rates since March 2020. The Bank of England has signalled that monetary policy will need to remain restrictive until risks to inflation returning sustainably to its 2% target in the medium term have subsided. Market expectations are for rates to fall further by the end of 2024 to 4.7%. **Figure 1.5** sets out the changing market expectations for the Bank Rate at various points from July 2023 to July 2024.

Figure 1.5

Future UK Bank Rate expectations

Based on average implied forward market interest rates (percentage). Actual value for the UK Bank Rate (solid grey line).

Sources: Bank of England



Interest rates have declined in the US and the Eurozone over 2024, with the Federal Reserve reducing rates to 4.75% - 5% and the European Central Bank reducing the deposit rate (its main interest rate) to 3.5%. Whilst high interest rates can weigh on economic activity, Jersey's banking sector has benefited from a period of sharp increases in interest rates with wider margins between lending and deposit rates leading to rapidly increasing profits. As rates begin to fall, bank profits will grow at materially slower rates. For households, mortgage holders on variable, tracker or ending fixed rate mortgages will benefit, whilst households with savings will see a lower return.

1.2 Jersey economic developments

The Budget has been brought forward relative to previous years and the Panel's Annual Report has been drafted in September 2024 before the publication of the 2023 GVA statistics. This has made it more difficult than in previous years for the Panel to assess the performance of Jersey's economy. The Panel has, however, been able to draw on the Business Tendency Survey

(BTS) and other data and information. The Panel recommends improvements are made to the frequency at which GVA data is produced as this is essential to enable a full assessment and understanding of the performance of Jersey's economy.

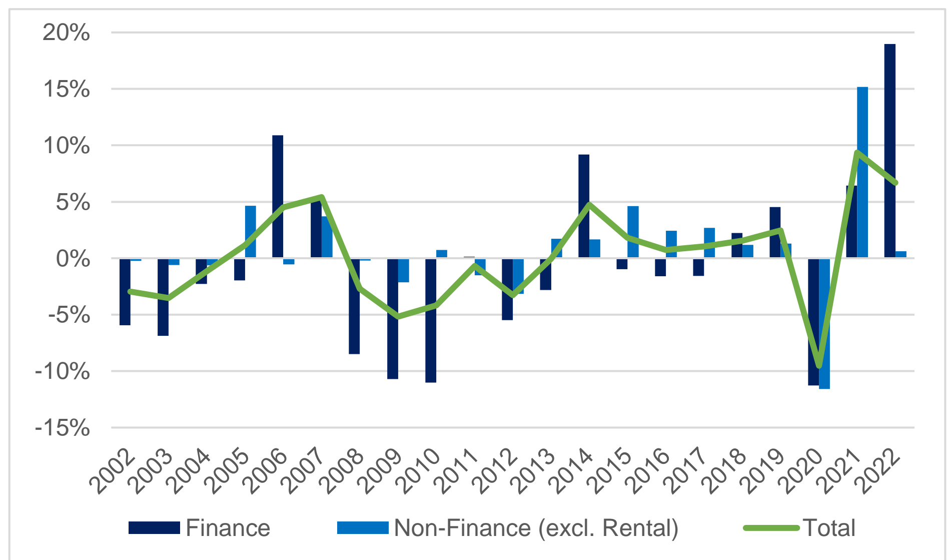
Jersey's economy grew by 6.7% in real terms and at basic prices[1] in 2022 (**Figure 1.6**), a faster rate than other advanced economies. This was driven by strong profits in financial services – specifically in the banking sub-sector, whilst the rest of the economy grew at a very modest pace. Indications are that Jersey's economy is likely to have grown strongly in 2023 before slowing in 2024. Jersey Incorporated Banks experienced strong profit growth in 2023 (**Figure 1.8**) – this is due to increases in net interest margins afforded throughout 2023 and is likely to have driven overall economic growth.

Figure 1.6

Jersey GVA growth

Annual percentage real terms change.

Source: Statistics Jersey



Strong profits in the banking sub-sector also drove real productivity growth of 4.9% in 2022. The non-finance sector saw productivity fall by -1.7%.

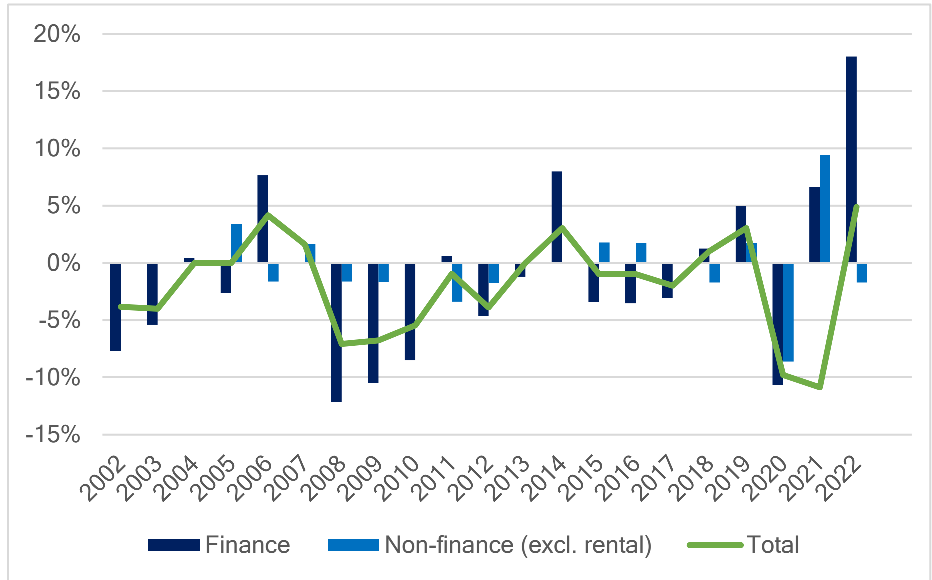
[1] Statistics Jersey published their report on 'Measuring Jersey's economy: GDP and GVA - 2022' on 4 October 2022. The publication introduced changes to the methodology and the headline measure of GVA. Changes include updating the classification of businesses into relevant sectors to the UK standard industrial classification 2007 system and presenting the values in market prices (previously in basic prices). For continuity, the FPP has presented the information under the "old" methodology, unless otherwise specified, to allow for an easier comparison to previous reports and economic assumptions.

Figure 1.6

Productivity growth

Annual percentage change in GVA per FTE in real terms.

Source: Statistics Jersey



1.2.1 Finance Sector

The financial services sector has been experiencing a period of strong growth (19% increase in real GVA in 2022). This was driven entirely by the banking sub-sector benefiting from an increase in net interest income (the difference in interest rates charged to borrowers and paid to deposits) and was caused by interest rates in the UK, US and EU increasing at the fastest rate for decades, reaching levels not seen since before the 2008 global financial crisis.

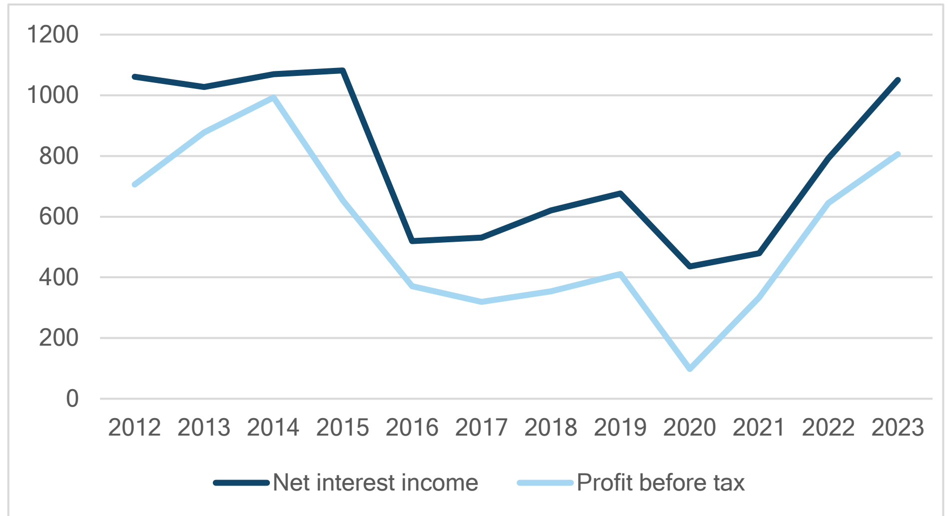
Figure 1.7 shows how the increase in net interest income has driven up profits for Jersey's banks, with net interest income increasing by 33% in 2023 to reach £1.05 billion. Despite cuts to base rates in the UK, US and Eurozone in 2024, base rates remain at a level that allows banks to achieve a net interest rate margin and strong profits. The Panel assesses financial services sector profits growth to have been very strong in 2023 at around 40% but expects it to fall back to around 6% in 2024 and 4% in 2025 and thereafter, modestly above the long-term trend of 3.2% (see **Figure 1.20**).

Figure 1.7

Jersey Incorporated Banks: Net interest income and Profit before tax

Net Interest Income and Profit Before Tax (£ million)

Sources: Jersey Financial Services Commission



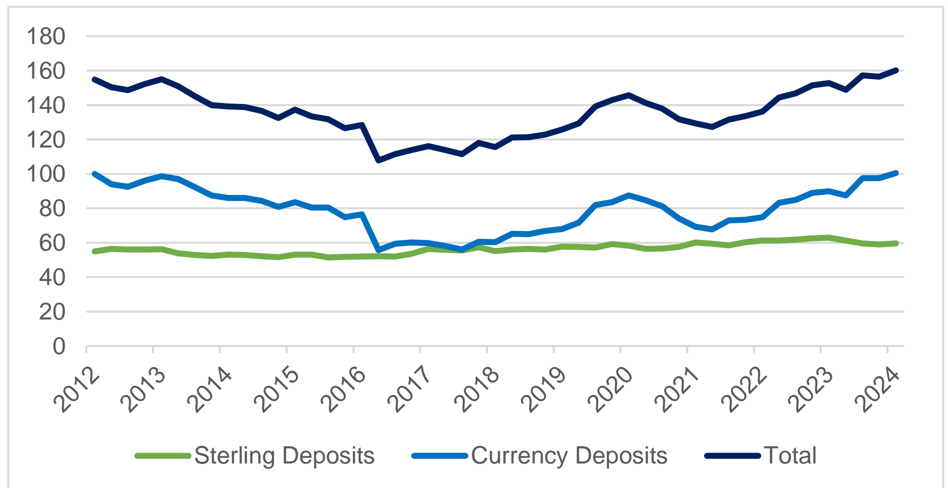
Increasing deposit levels as well as rising interest rates have contributed to strong profit growth for Jersey's banks. The total value of deposits (**Figure 1.8**) held by Jersey banks was over £150 billion in Q1 2024, of which an increasing share is being accounted for by foreign currency deposits (including in dollars and euros).

Figure 1.8

Banking deposits

Total bank deposit values (£ billion current prices) in sterling and foreign currencies ("Currency Deposits")

Sources: Jersey Financial Services Commission



The **Business Tendency Survey (BTS)** from June 2024 indicates business sentiment within the finance sector remains positive. The headline business activity indicator (which in the past has been a good indicator of GVA growth) is stable compared to the corresponding period last year, with the weighted balance of firms reporting an increase in current business activity and future business activity outweighing those who reported a decrease.

In July 2024, Jersey received a successful MONEYVAL report following the Council of Europe's monitoring body assessment to determine the effectiveness of the Island's anti-money laundering and counter-terrorist financing measures. The report placed Jersey's effectiveness in preventing

financial crime among the highest level in all jurisdictions globally. This may further improve the attractiveness and performance of Jersey's financial sector.

1.2.2 Rest of the economy

Whilst the finance sector performed very strongly in 2022, this is in stark contrast to the rest of Jersey's economy which experienced weaker growth of just 0.6%. Business survey indicators suggest that business activity weakened in 2023 and into 2024 (**Figure 1.9**). This would be consistent with further weakening of growth in the non-finance sectors compared to 2022. The input costs indicator remained strongly negative, suggesting local businesses continue to experience inflationary pressures. Concerns about profitability may also be having a negative effect on business optimism.

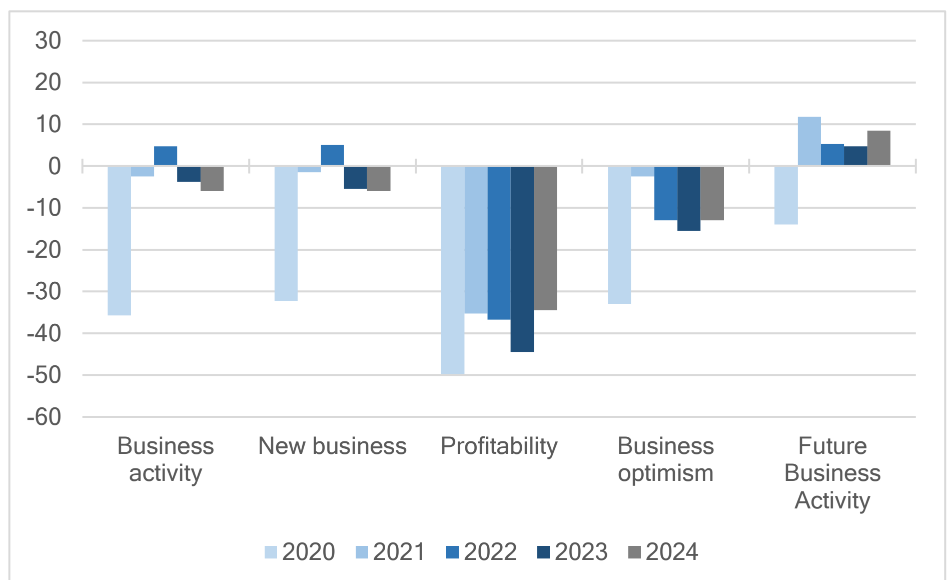
Figure 1.9

Non-finance business tendency

Percentage net balance of respondents reporting an increase (weighted by employment). Average of quarterly results

Note: 2024 covers March and June.

Sources: Statistics Jersey, Panel calculations



1.2.3 Sectoral performance of the non-finance economy

Business activity in the **wholesale and retail** sector fell in 2023 compared to 2022, as indicated by the BTS. Responses to the BTS in 2024 have remained largely negative, particularly with respect to input costs and profitability. Continuing challenges to the sector include the increasing cost of inputs (which might include the increases in the Minimum Wage) as well as the cost-of-living pressures on consumers, which are likely to have impacted discretionary spend.

According to the BTS, the **hotels, restaurants and bars** sector experienced weakening business activity and profitability in 2023 following strong post-pandemic recovery in 2022. In 2024, survey responses relating to capacity utilisation and employment have worsened, suggesting current growth may be

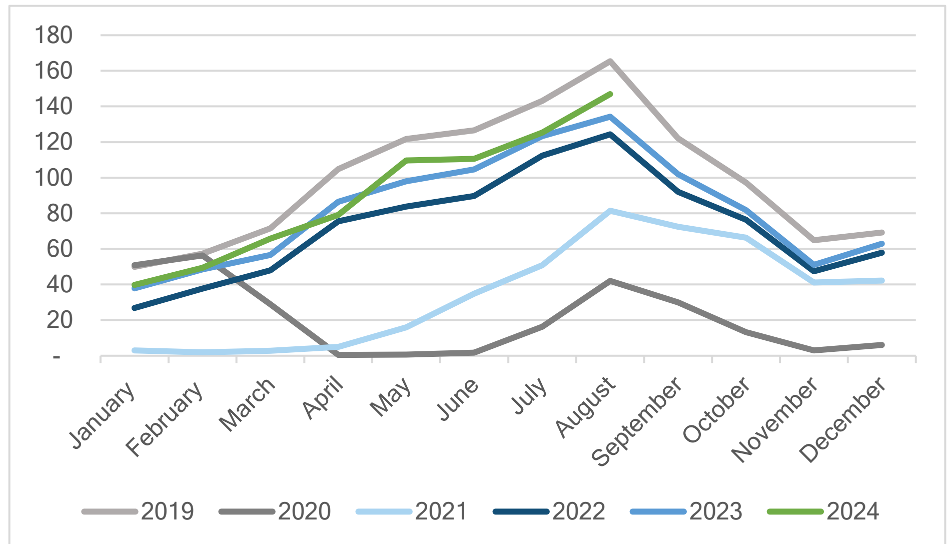
weak. **Figure 1.9** shows that departures are increasing year-on-year, with departures from January – August 2024 5% higher than the same period in 2023. However, departures remain below pre-pandemic levels.

Figure 1.9

Port departure numbers

Number of departures from Jersey air and sea terminals (thousands)

Sources: Ports of Jersey



The BTS shows rising costs continue to affect the **construction** sector with lower profits, capacity utilisation and employment also becoming significant issues over the last 18 months. The recent slowdown in the housing market has likely lowered demand for construction companies, however the indicator for future business activity was positive in the most recent survey, suggesting that the sector may be expecting market recovery. (see **Section 1.5**).

1.3 Labour Market

Jersey's economy is labour intensive, and the labour market typically operates at full employment. Additional and seasonal jobs are filled by recruitment from overseas. Prior to 2020 many of these seasonal workers came from or via the UK, but now increasingly these seasonal workers come from further afield. This means that recruitment is less flexible and responsive, having to be planned ahead of time and based on estimates of need or business activity. In turn this makes it more difficult to match workers to actual business activity and optimise capacity utilisation. Further, overseas workers on work permits are typically restricted to work for the employer that recruited them. These features of the labour market may explain why the BTS simultaneously shows both employment growth and spare capacity within sectors and why certain sectors have spare capacity whilst others have insufficient capacity. This is suggestive of a labour market that is not functioning as well it might because labour market flexibility has been reduced.

In 2023 Jersey's economy created an additional 700 jobs to take the total number of jobs to 64,200 by December 2023, the highest recorded December total (**Figure 1.10**). Jobs filled by entitled workers fell by 0.9% whilst the number of jobs filled by migrant workers increased by 14.6%.

Figure 1.10

Labour force composition

Total numbers of jobs filled by workers registered as entitled and migrant (includes those in the licensed, registered and exempt categories)

Sources: Statistics Jersey

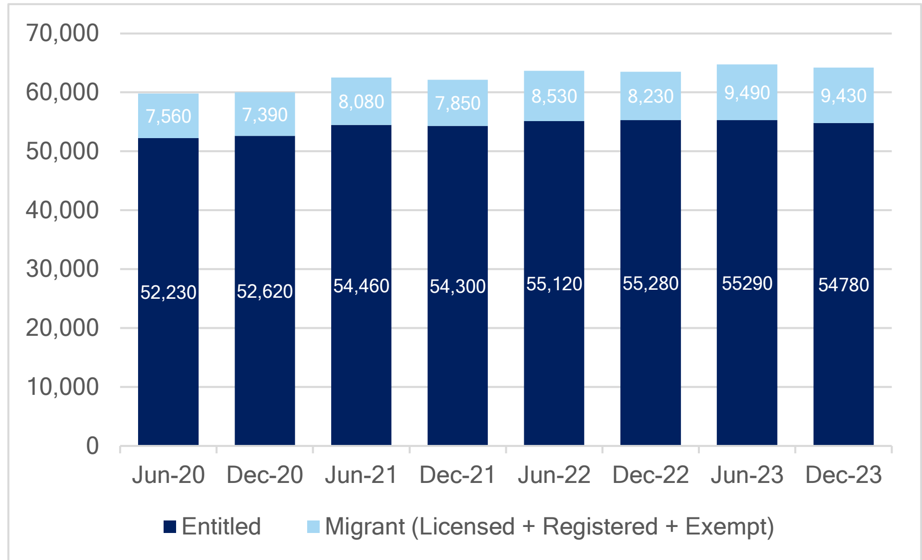


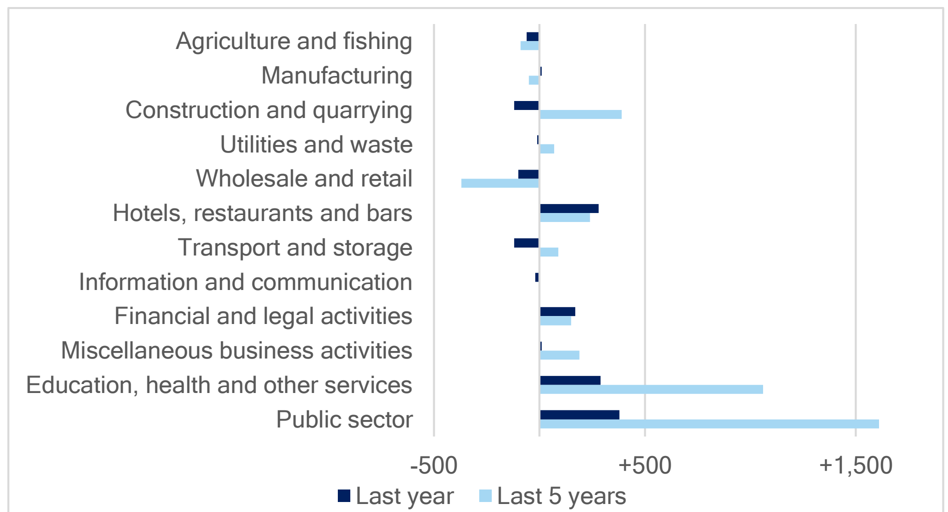
Figure 1.11 breaks down the growth in jobs by industry. In 2023, job growth was primarily driven by the public sector (+4.2%), hospitality (+5%) and private sector education & health (+3%). These industries have also driven job growth over the past 5 years, alongside construction, which experienced a fall in jobs in 2023. Notably, the number of jobs in hospitality is now greater than in December 2019, prior to the Covid-19 pandemic. Some industries have seen decreases in employment over the past 5 years, namely wholesale and retail (-5%), agriculture and fishing (-10%) and manufacturing (-5%).

Figure 1.11

Change in jobs by industry

Change in total jobs by sector, Dec 2022 - Dec 2023 and Dec 2018-Dec 2023; "education, health and other services" covers private sector education and health only

Sources: Statistics Jersey



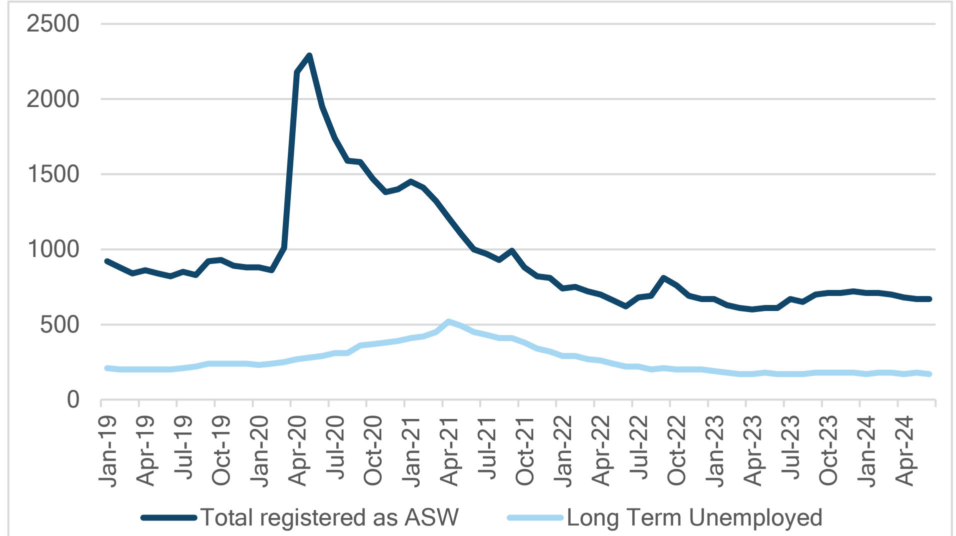
Unemployment has remained relatively low and stable since 2022 (**Figure 1.12**). Latest data from June 2024 indicates that the number of people registered as actively seeking work (ASW) was 670, slightly higher than twelve months earlier but around 200 less than pre-pandemic levels. The number of long-term unemployed was stable relative to a year earlier.

Figure 1.12

Individuals Actively Seeking Work

Number of those registered as Actively Seeking Work on the last calendar day of each month. Long term Unemployed relates to those which have been registered as Actively Seeking Work for over 12 months.

Sources: Statistics Jersey / Customer and Local Services



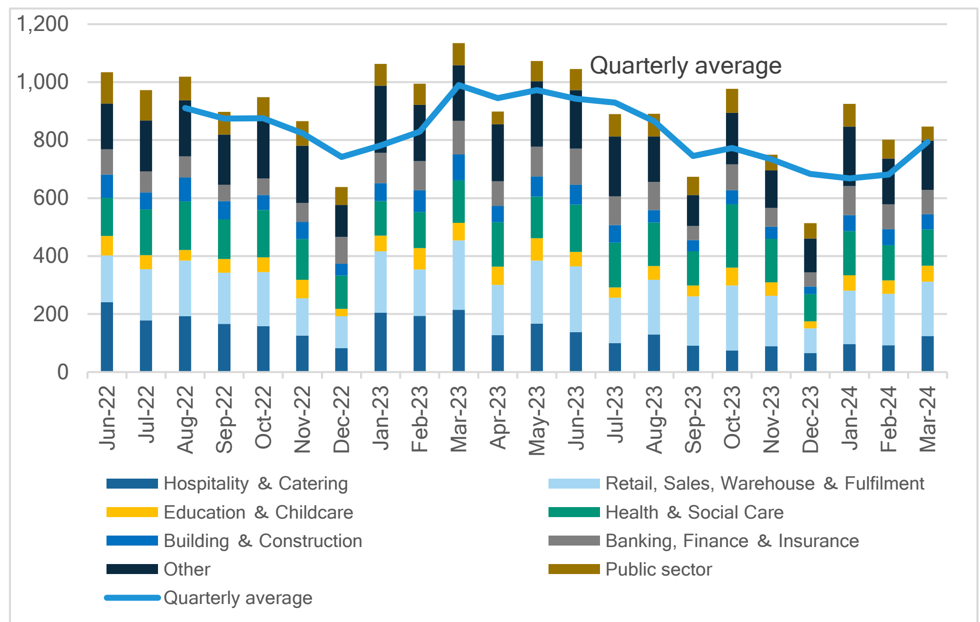
Data on vacancies indicates that growth in the labour market may be slowing. **Figure 1.13** shows vacancy postings on the Government of Jersey website by industry, with total job vacancy postings in Q1 2024 19% lower than Q1 2023.

Figure 1.13

Vacancies in Jersey

Number of private sector vacancies by sector posted on the Government of Jersey website. Postings on the site can be given three sector categories; for this chart, vacancies are assigned to the first sector listed. Postings with no sector listed are excluded

Sources: Customer and Local Services



The breakdown of vacancy postings across industries has remained broadly stable since 2022, with the highest number of vacancies in retail, health & social care and hospitality. Notably, the share of vacancies accounted for by hospitality has fallen from 19% of postings in Q1 2023 to 12% in 2024. This

may reflect changes in demand following job growth in hospitality in 2023 or changing recruitment practices for the industry.

Growth in nominal earnings has remained strong following a period of high inflation and low unemployment, with average earnings rising by 6.5% in the year to June 2024 (**Figure 1.14**). Public sector average earnings increased by 8.8%, driven by a headline pay award of 8% and nurses and teachers receiving delayed pay awards from 2023, whilst private sector average earnings increased by 5.9%. Lower earners have benefited from an increase to minimum wage from £10.50 in January 2023 to £11.64 in January 2024 (10.9%), contributing to higher-than-average earnings growth in the hospitality and wholesale & retail sectors.

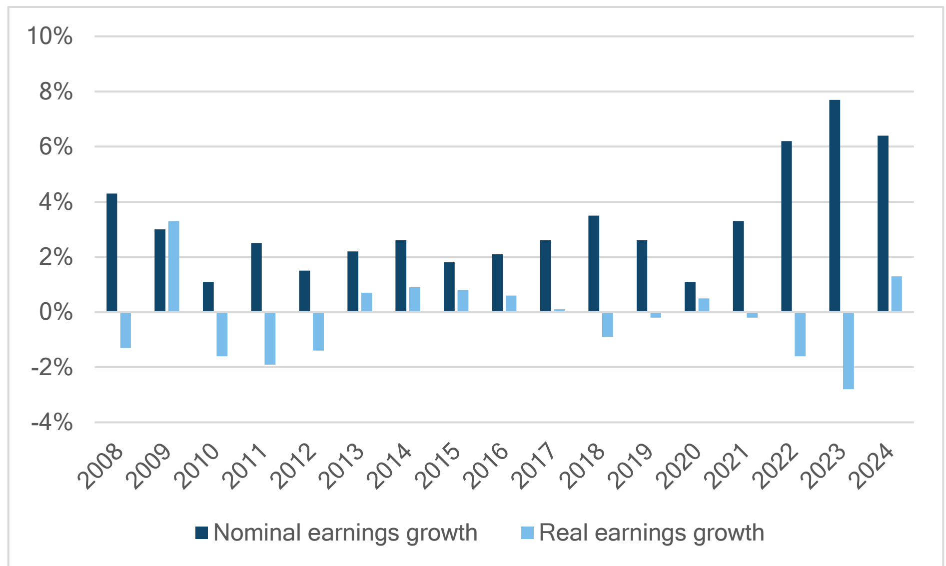
Average earnings in 2024 increased in real terms for the first time since 2020, by 1.3%. However, from 2021 to 2024, average earnings have decreased by 3.1% in real terms, reflecting high inflation in 2022 and 2023. Together with higher mortgage costs (from higher interest rates) this may go some way to explain the reduction in business activity in sectors such as hospitality.

Figure 1.14

Nominal and real terms average earnings, percentage change

Percentage change in nominal average earnings (dark blue) and real terms average earnings (light blue).

Sources: Statistics Jersey



1.4 Inflation

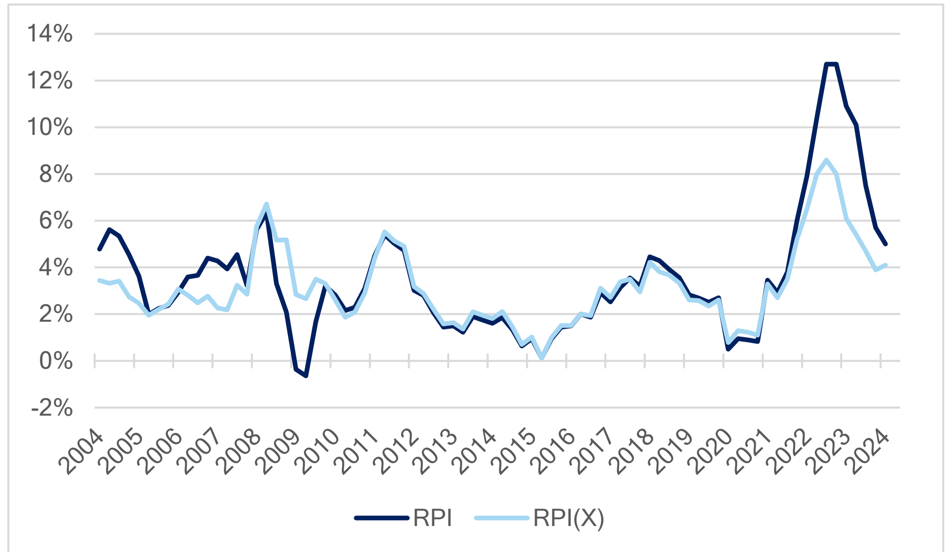
Jersey's headline measure of inflation, the Retail Price Index (RPI), was 5.0% in June 2024, falling from 10.9% in the same period a year ago (**Figure 1.15**). RPI(X), which excludes mortgage interest payments, was 4.1%, rising slightly from the previous quarter but down compared to a year earlier when it was 6.1%. Falls in inflation have been driven by interest rates flattening off and thus contributing to slower rises in housing costs for households with mortgages, and also by lower imported inflationary pressures from the UK due to falling energy prices.

Figure 1.15

Inflation in Jersey

Annual percentage change in retail prices index (RPI) and retail prices index excluding mortgage interest payments (RPI(X))

Sources: Statistics Jersey



1.5 The housing market

House prices in Jersey have historically increased faster than both RPI and average earnings (**Figure 1.16** shows how house prices, inflation and earnings have changed since 1990). However, high interest rates contributed to a slowing housing market in 2023, with house prices falling for the first time since 2013 (by 3%), whilst RPI and earnings grew.

Figure 1.16

House Price, Retail Prices and Average Earnings Indices

Index 1990 = 100

Sources: Statistics Jersey

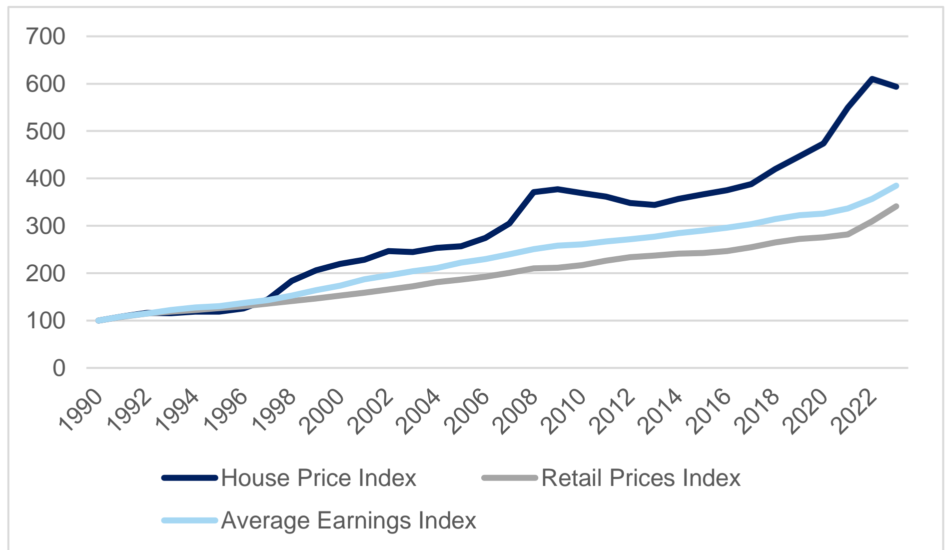


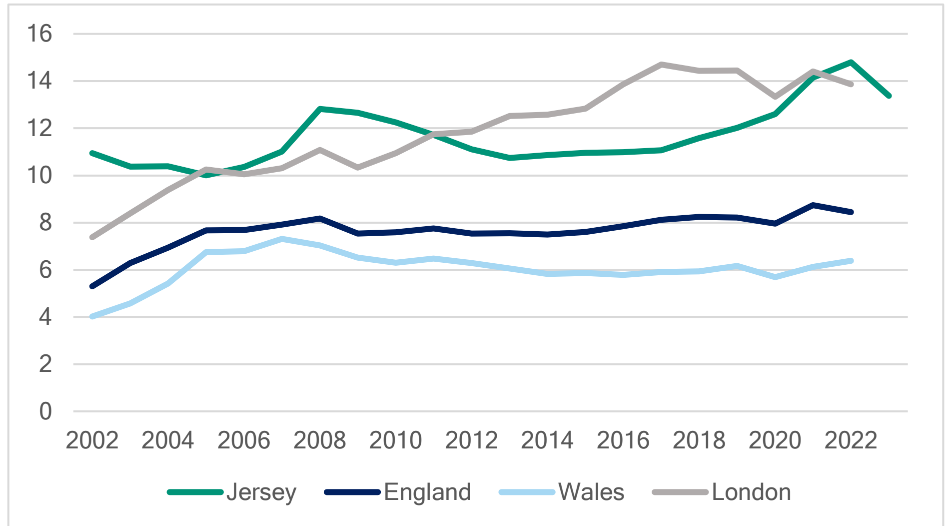
Figure 1.17 compares the house price to income ratio in Jersey with areas of the UK. Reflecting falling house prices and rising incomes, the house price to income ratio in Jersey improved in 2023. However, the average house price is still over 13 times average net household income, and this is in the context of households facing high mortgage interest rates.

Figure 1.17

House price to income ratio - comparison with the UK

Ratio of median property price to equivalised median net household income, 2002-2022

Sources: Statistics Jersey, UK Office for National Statistics



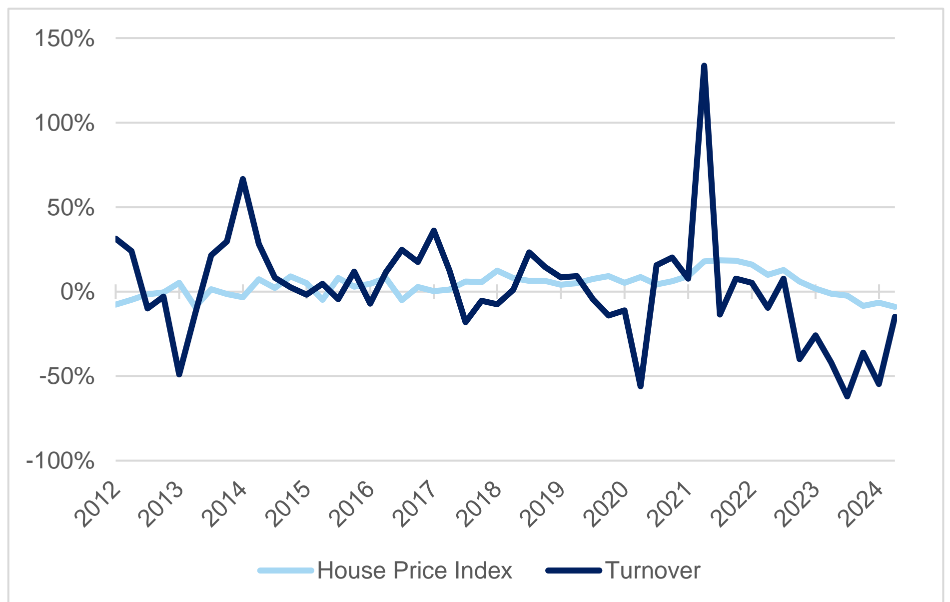
Housing market activity has continued to fall in 2024, with latest quarterly data indicating a decrease in turnover of 15% in Q2 2024 compared to Q2 2023 (**Figure 1.18**), despite a slight uptick compared to the previous quarter. House prices have also fallen, with prices in Q2 2024 9% lower than Q2 2023. However, when comparing to 2023 data it is important to note that 2023 saw a significant proportion of transactions (39%) that were the completions of off-plan purchases in new developments – excluding these, which can be erratic, prices and turnover would have fallen further in 2023.

Figure 1.18

Housing market

Annual change in House Price Index and transaction numbers

Sources: Statistics Jersey



Many households on fixed rates have been protected from higher mortgage costs (with 73% of household mortgages in 2021/22 on fixed rates). For example, according to Bank of England data, the interest rate on a standard 5-year fixed rate mortgage with a 75% loan-to-value ratio has increased from 1.9% in July 2019 to 4.5% in July 2024. As households refinance, their

mortgage payments will significantly increase, causing some to cut back non-housing expenditure or fall into mortgage arrears, with consequences for the rest of the economy.

The 2024 Government Plan included a £10 million shared equity pilot scheme to help first-time buyers ("First Step"). Transactions through this scheme began from June 2024 and once complete, it is expected to help up to 60 households achieve home ownership. Budget 2025 proposes a further £2 million to the scheme. It is too early to estimate the full impact of the scheme. However, **the FPP continues to recommend that the impact of the pilot scheme on the housing market should be carefully monitored before the Government considers or develops extensions to the scheme.**

Earlier this year, the Panel published a review of Jersey's housing market, looking at the performance of the housing market over the last 15 years, contributing factors, and the economic impact. The review noted that Jersey faces similar issues to other rich economies where spending on housing is high as a proportion to income. Coupled with relatively high income-inequality (and a lack of borders), this makes market rents and house prices unaffordable for a considerable portion of the population.

1.6 Economic growth forecast

In May 2024, the latest FPP economic assumptions were published. Real GVA is judged to have grown by 9.3% in 2023, driven by strong profit growth in the banking sector. Real GVA growth is forecast to slow to 2.1% in 2024 and 0.5% in 2025, reflecting slower expected growth in financial sector profits. Average earnings and employment are expected to grow steadily over the assumptions period.

In May, the Panel forecast RPI annual inflation at 3.5% in 2024 (**Figure 1.19**). This follows a trend of falling inflation rates from a peak of 12.7% in March 2023. However, recent price data collected in Q2 2024 showed RPI was 5.0%, suggesting inflationary pressures are persisting. This may indicate overheating in the economy. The Panel will continue to monitor inflation rates closely.

Figure 1.19

Inflation forecast (RPI and RPI(X)), May 2024

Blue line is RPI, green line is RPI(X). Dotted lines indicate forecasts.

Sources: Statistics Jersey, Panel calculations

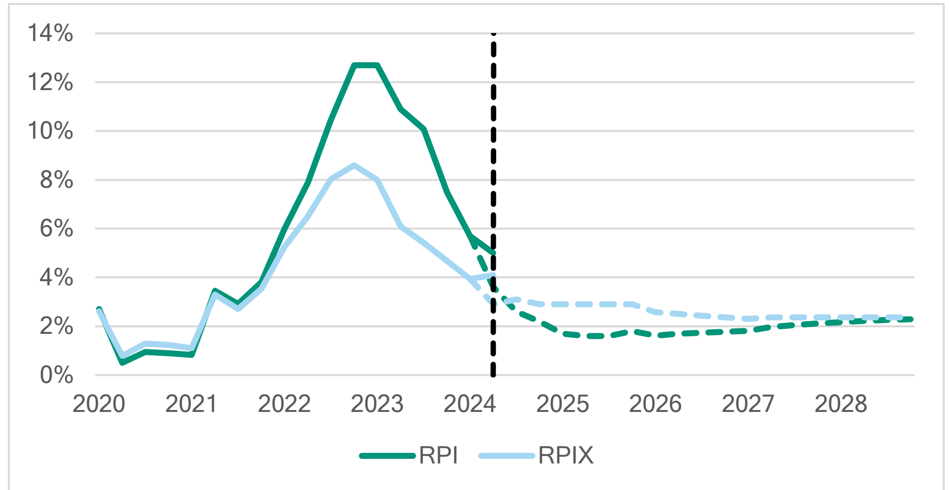


Figure 1.20

Central Economic Assumptions, May 2024

Percentage change year on year unless otherwise stated, light blue indicates outturn data.

Note: changes in profits, earnings, employment costs and house prices are in nominal terms.

Real GVA is deflated with RPI(Y), however, the rental component of GVA is deflated with a separate rental deflator.

Sources: Statistics Jersey, Panel calculations

% change unless otherwise specified	2021	2022	2023	2024	2025	2026	2027	2028	Trend
Real GVA	9.4	6.7	9.3	2.1	0.6	0.8	0.8	0.8	0.5
RPI	2.7	9.3	10.2	3.5	1.7	1.7	2.0	2.2	2.4
RPI(X)=RPI(Y)	2.7	7.1	6.0	3.2	2.9	2.5	2.4	2.4	2.4
Nominal GVA	12.3	14.7	16.1	5.3	3.2	3.0	2.9	3.0	2.9
Gross operating surplus (including rental)	20.4	23.8	23.6	4.7	3.1	3.0	2.9	3.0	2.9
Financial services profits	*13.1*	*49.4*	*40.0*	*6.0*	*4.0*	*4.0*	*4.0*	*4.0*	*3.2*
Compensation of employees (CoE)	6.3	7.2	9.0	6.0	3.4	3.1	2.9	2.9	2.9
Financial services CoE	*5.9*	*6.1*	*7.3*	*5.4*	*3.4*	*3.4*	*3.4*	*3.4*	*3.4*
Non-finance CoE	*6.3*	*7.8*	*9.1*	*5.1*	*3.3*	*2.9*	*2.8*	*2.8*	*2.7*
Employment	2.9	2.8	1.4	0.5	0.4	0.4	0.4	0.4	0.1
Average earnings	3.3	6.2	7.7	5.2	3.0	2.6	2.4	2.5	2.8
Interest rates (%)	0.1	1.5	4.7	5.1	4.6	4.1	3.8	3.7	3.3
House prices	16.0	11.0	-2.6	0.0	2.0	2.0	3.0	3.0	2.9
Housing transactions	15.1	-12.9	-42.9	12.0	30.0	23.0	1.0	1.0	4.0

*Trend interest rates represent market expectations for 2028

1.7 Risks to growth

In the absence of GVA data for 2023, the Panel's assessment of the indicators available is that growth remained strong in 2023. As in 2022, this is likely to have been primarily driven by net interest related profits in the banking sector. Jersey's banks have strongly benefited from the sharp rise in interest rates in 2022 and 2023 but as interest rates stabilise and begin to come down, profits growth is projected to slow in 2024 and thereafter. However, the outlook for the sector is likely to have been enhanced by a recent MONEYVAL assessment, which concluded that the Island's effectiveness in preventing financial crime was among the highest found in jurisdictions evaluated globally. The sector will also be affected by the introduction of the OECD Pillar Two global minimum tax framework. All else equal, this should result in higher

tax revenues from the sector due to the higher tax rate; however, the impact of the framework on the relative attractiveness of Jersey as a financial centre and on the non-banking sector is uncertain and a source of risk.

Recent survey data indicates growth has weakened further for non-finance sectors, with a more negative outlook for sectors such as hospitality and retail. Such a divergence between banking and the rest of finance and the non-finance sectors of the economy risks long-term sustainable growth on the Island.

1.8 Other economic risks

Continuing elevated inflation poses a risk to Jersey's economy, with inflation in Q2 2024 higher than forecast. Whilst headline inflation is likely to continue falling in the near term as the reduction in interest rates feeds through to lower housing costs, the rise in underlying inflation (RPIX) coupled with BTS data on input and product prices indicates that inflationary pressures remain across the Island. These could become a greater concern in the coming months, particularly if the planned increases in the minimum wage, to bring it to a living wage, are not accompanied by offsetting productivity increases.

The outlook for the global economy has remained stable for 2024, though risks on inflation have become more pertinent. If inflation remains persistent in the UK, or trade or geopolitical tensions result in price shocks, this could add to inflationary pressures in Jersey.

As recognised in the 2023 Strategy for Sustainable Economic Development, Jersey faces the twin challenges of low productivity and maintaining living standards with an ageing population. Since 1998, productivity in Jersey has fallen by around 30%. Declining productivity has a direct impact on living standards – through declining real earnings and business profits.

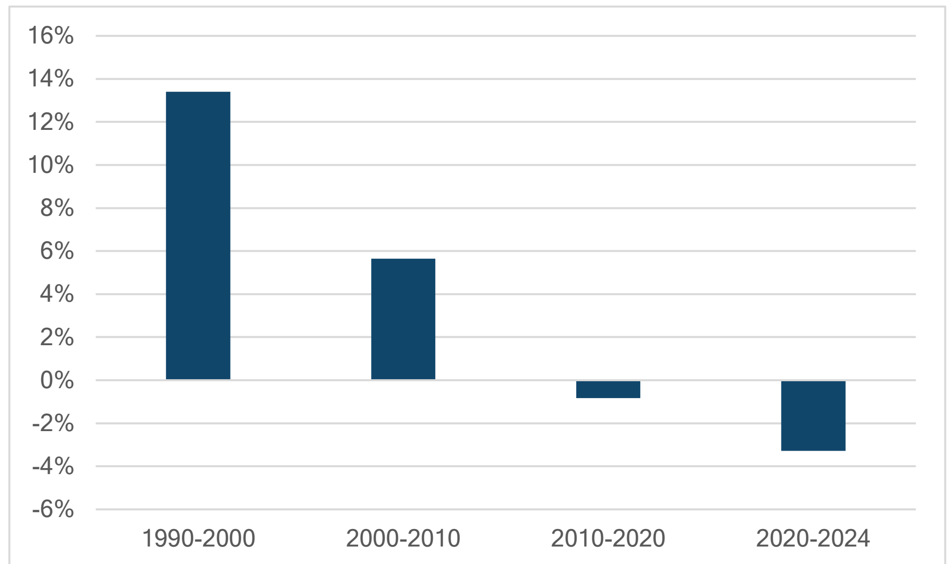
Figure 1.21 shows how real earnings have changed since 1990. Higher productivity growth in the 1990s was accompanied by real earnings growth, with living standards increasing. However, since 2010 real earnings have declined.

Figure 1.21

Real earnings percentage change over 10-year periods, 1990 – 2024.

10-year percentage change in average real earnings, 1990 - 2020. Current period includes change from 2020-2024.

Sources: Statistics Jersey



Lower earnings and profits per capita also put pressure on constrained Government finances for public services. This is compounded by an ageing population. To provide the tax revenues to support a much larger older population, to maintain Jersey's competitiveness as a jurisdiction and to mitigate and adapt to a changing climate, economic growth needs to come through higher productivity. **The Panel reiterates the importance of addressing the challenge of declining productivity in an ageing population as a priority to maintain living standards and to minimise the constraints these challenges place on the fiscal position.**

The Fiscal Outlook

2.1 Introduction

This section considers the proposed Budget 2025-28 ('the Budget') and assesses the extent to which it follows the fiscal framework guidelines. The Budget was lodged in August 2024 and is scheduled for debate by the States Assembly on 26th November 2024.

As set out in the Economic Outlook, Jersey's economy grew strongly in 2022 driven by a sharp increase in banking profit. All the indications are that this growth continued in 2023. The Panel expects economic growth to slow materially in 2024 and to be below 1% annually from 2025 onwards.

In its May 2024 Economic assumptions (FPP Spring 2024), the Panel revised up its expectations for 2023 banking profits and economic growth. In turn this has led to upward revisions in the forecast for Corporate Income Tax revenue in 2024. Despite this, the Budget will be in an operating deficit in 2025 and 2026 due to significant increases in current expenditure. The proposed increase in current spending budgets has required savings across Government departments to help fund the expenditure growth. In addition, reserve funds are also being used to finance short-term policies introduced in the Budget.

Proposed Budget 2025-28

The Budget proposes:

- A 1% increase in States income of £47 million over 2025 – 2027 compared to Government Plan 2024, generated by higher forecast tax receipts. Across the Budget States income will total £5.268 billion.
- A 3% increase in expenditure of £103 million over 2025 – 2027 compared to Government Plan 2024 - this is net of a proposed saving programme worth £47 million per annum.
- Allocating £29 million to fund the Government's Common Strategic Policies ('CSP') and an additional £31 million annually (£124 million total) funding for the Health and Community Services Department ('HCS') across 2025 – 2028.
- Spending increases of £97 million to help meet inflationary pressures from 2025 – 2028.
- The operating balance will be in deficit in 2025 (- £18 million) and 2026 (- £1 million), with a surplus in 2027 (+ £10 million) and 2028 (+ £18 million. Across 2025 – 2027, Government Plan 2024 forecasted a total operating surplus of £52 million, under Budget 2025 this will move to a total deficit of - £9 million over the same period.

- Total reductions of £21 million across capital budgets, compared to Government Plan 2024, to help 'right-size' the capital programme and make projects more deliverable
- A financing strategy for Phase 1 of the New Healthcare Facility. This includes £523 million of public borrowing and up to £277 million of transfers from the Strategic Reserve.
- The Pillar Two 'base case' forecast, which anticipates additional Government revenue of £52 million annually (from 2026), This additional revenue has not been included in the forecast for general income.

In assessing the Budget, the Panel is guided by its five guiding principles:

1. Economic stability is at the heart of sustainable prosperity;
2. Fiscal policy needs to be focused on the medium term;
3. Policy should aim to be predictable, with flexibility to adapt to economic conditions to assist in creating a more stable economic environment;
4. Supply in the economy is as important as demand; and
5. Low inflation is fundamental to the competitiveness of the economy.

The Panel also comments on how the Budget follows the Fiscal Framework outlined in *Establishment of a Stabilisation Fund and Policy for the Strategic Reserve (October 2006)* – legislation passed by the States Assembly setting out the following objectives of fiscal policy:

- 'Create an effective macroeconomic policy framework that can improve economic stability by containing inflation and maximising the economic potential of the Island'
- 'Put in place a transparent and credible framework that is both pragmatic and understood by everybody in the Island'
- 'Make fiscal policy overall more counter-cyclical and manage the revenue streams in a manner that enhances economic performance'

The Fiscal Framework is specifically concerned with the role of the **Strategic Reserve,** which should include enough capital to insulate the Island from severe structural decline or major natural disasters and only be used in these instances, as well as the **Stabilisation Fund** which should enable counter-cyclical fiscal policy to create a more stable economic environment with low inflation in the Island.

2.2 Income tax forecast

The Budget shows an increase in forecast tax revenue in 2025 and 2026 **(Figure 2.1)**, with a slight reduction in 2027 when compared to the previous Government Plan; the net effect is an additional £33 million over 2025 - 2027. This increase has been driven by forecast higher growth in banking profits.

In May 2024, the Government announced it would adopt the OECD Pillar Two tax regime from 2025. This will introduce a 15% minimum tax framework to multi-national enterprises with annual global revenues of at least €750 million and is expected to generate additional corporate income tax revenue for Jersey. This global tax change can be expected to create some uncertainty and could negatively affect the competitiveness of large businesses in Jersey and some behavioural change can be expected. Given the uncertainty about how much additional tax revenue will be raised by Pillar Two in the short and medium term, the Panel supports the decision of the Government in not including Pillar Two tax revenues in its main forecast and in not using these to fund expenditure. It also supports the Budget proposal that any upside additional revenues from Pillar Two, above the base forecast, should not be spent on recurring items but should be used for strengthening reserves and investing for the medium-term. The Panel recommends that this proposal is made into a commitment.

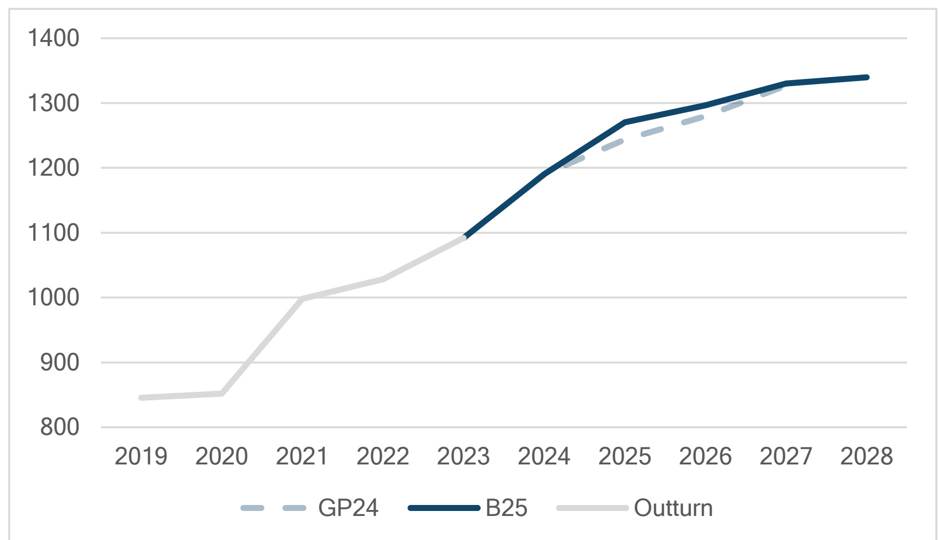
Figure 2.1

General Income forecast May 2024

£ million

This includes the central tax forecasts as well as other budget measures

Source: Treasury and Exchequer



2.3 Government expenditure

The Budget proposes a net increase of £103 million in current expenditure across years 2025-2027. This additional expenditure is being used to fund the delivery of the CSP, create provisions to meet future inflation pressures, fund 'formula driven' budget increases and address ongoing deficits in the Health and Community Services (HCS) department **(Figure 2.2).** The inflation provisions are, in part, to fund the 3-year public sector pay settlement of RPI +1%.

Figure 2.2

Categories of New Expenditure Growth

£ million

79% of new expenditure growth is being committed to Health budgets. The spend on CSP is distributed across different policies - examples include, free school meals, extended nursery provision and education programmes.

Source: Treasury and Exchequer

	2025	2026	2027	2028
CSP	6	8	7	8
HCS	**31**	**31**	**31**	**31**
Non-Ministerial	2	3	3	3
Total	**39**	**42**	**41**	**42**

2.3.1 Savings

The Budget includes proposed annual savings of £47 million that will be made from non-frontline budgets (target to be met by 2027). The panel notes that relying on future savings to fund planned expenditure is not without risk.

Over the Budget period, £17 million of savings are expected from the Financial Recovery Programme (FRP), which aims to deliver a more efficient and value for money health service. The FRP has already realised £8 million in savings, and the previous Government Plan anticipated that in total £25 million would be fully realised by 2025, the current Budget now expects that this target will not be delivered until 2026.

In addition, £15 million of savings are planned through a reduction in non-frontline Government roles. This is a CSP commitment to help 'curb the growth in the public sector' and increase efficiency. Part of this target will be generated by reducing the use of external consultants, contractors and professional advisors, whilst ensuring frontline roles are protected. Centralising civil service functions in the new Government Headquarters building is expected to save a total of £4 million in rent and other office costs. 'Future Savings' of £4 million (9% of the total savings targets), are yet to be

allocated to specific departmental budgets **(Figure 2.3)**. The FPP reiterates its previous advice and cautions against relying on future unspecified savings.

Figure 2.3

Breakdown of Saving Proposals

£ million **(current prices)**

A reduction in non-front line Government roles is proposed to deliver the most significant savings outside FRP. Savings on office costs and non-ministerial bodies will deliver less than £1 million in some years.

Source: Treasury and Exchequer

	2025	2026	2027	2028
Arm's length organisations	1	1	1	
Office costs	2	2	-	-
Growth reductions	3			
Role reductions	6	9		
Non-ministerial bodies	-			
FRP (HCS)	8	9		
Future savings (unspecified)		3	1	
Total	**20**	**24**	**3**	**-**

2.3.2 Inflation and Formula Driven Spending

£97 million has been allocated for inflation-driven expenditure growth over 2025 – 2028 **(Figure 2.4)**. Much of this is to meet 'pay' and 'non-pay' inflation pressures in Government Departments, £15 million of which relates to the 3-year public sector pay agreement that increases wages by 8% in 2024 and by RPI +1% in 2025 and 2026.

'Formula driven' growth accounts for a further £49 million over the Budget period. This includes expenditure that increases annually by pre-agreed formulae, such as:

- an annual 2% increase in Health budgets
- the Jersey Overseas Aid budget is equal to 0.3% of GVA by 2024
- the budget for Arts, Heritage and Culture is equal to 1% of Net Revenue Expenditure in 2024 and be increased by RPI annually thereafter
- grants made to the Social Security Fund and Long-Term Care Fund required by law

The Panel continues to recommend against the use of formula driven budget growth, and especially formula driven budget growth linked to GVA or net revenue. This risks creating spending targets that are inefficient and/or undeliverable. If the intention is to maintain a level of resources year-on-year then the Panel recommends that RPI should be used to grow budgets as in the case of the Arts, Heritage and Culture budget.

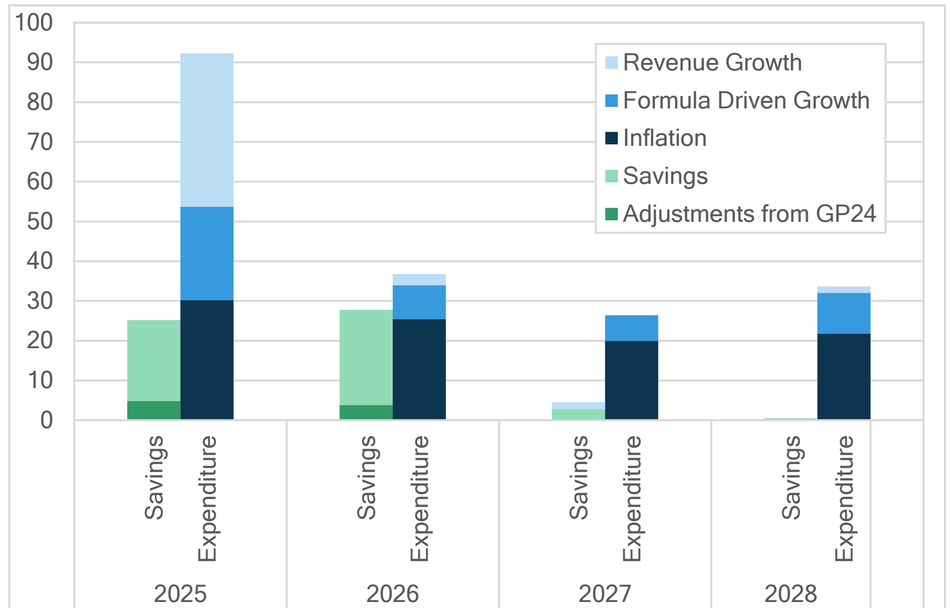
Figure 2.4

Expenditure growth by type vs Savings proposals

£ million

Light blue shows the value of new expenditure lines (revenue growth), blue shows the formula driven budget increases and navy blue shows the provisions for inflation driven spend. Green shows the total value of saving proposals.

Source: Treasury and Exchequer



Year on Year Net Expenditure Increases

£ million

Annual increases in net expenditure are being reduced by Savings

Source: Treasury and Exchequer

	2025	2026	2027	2028	Total
Adjustments from GP24	-4.9	-3.8	-0.2	0.0	-9
Savings	-20.3	-24.0	-2.5	0.5	-46
Inflation	30.2	25.4	19.9	21.8	97
Formula Driven Growth	23.4	8.5	6.5	10.2	49
Revenue Growth	38.7	2.8	-1.8	1.6	41
Net expenditure increase	**67**	**9**	**22**	**34**	**132**

2.3.3 Health and Community Services

76% of the total increase in current expenditure growth over 2025 - 2028 has been committed to the Department for Health and Community Services' budget ('HCS') **(Figure 2.2).** This equates to over £31 million in additional annual funding being allocated to address 'ongoing risks and pressures' in HCS. As a result, 27% of total Government expenditure in 2025 will be on healthcare spending. This is a societal and political choice. The Panel observes, however, that it is higher than an average of 16% across OECD members* (2022 figures) and that in other important areas of the economy, such as economic development or other public services, public expenditure in Jersey is significantly below the OECD average. Health spending per capita in Jersey was £3,983 in 2022, higher than the OECD average of £2,554* **(Figure 2.5).** Whilst this remains lower than the highest per capita, public spenders like the United States and United Kingdom, Jersey has a significantly smaller tax

base from which to fund Government expenditure. **Figure 2.5** illustrates that in 2022, Health was the only classification in which Jersey spent above the OECD average as percentage of GDP, whereas all other categories saw below average spending as a percentage of GDP (excluding environmental protection).

Moreover, healthcare costs can only be expected to increase in real terms over time, particularly in the context of an ageing population. **Spending pressures on health can be expected to increase and will require difficult choices to be made between funding for healthcare and growing other areas of the economy through investment into productive capacity.**

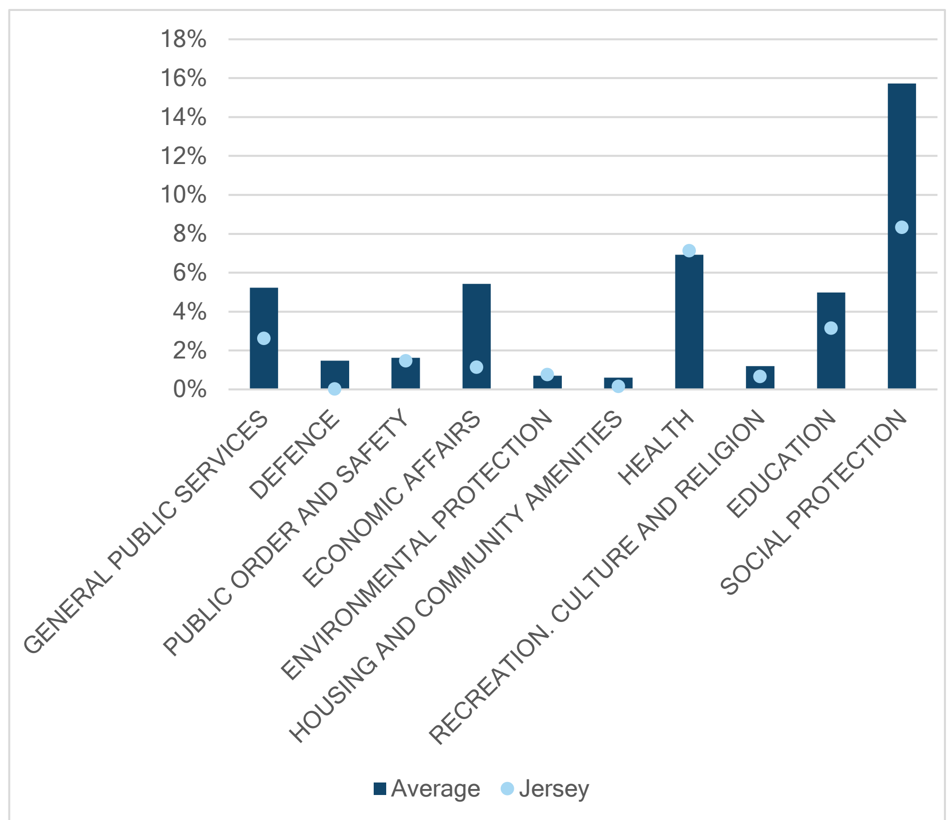
Figure 2.5

Classification of the Functions of Government - Jersey 2022 vs OECD 2022 average (spending as a % of GDP)

£ million (current prices)

The Classification of the Functions of Government (COFOG) breakdown public spending into different areas of Jersey's economy. Jersey statistics are compared to the published 2022 OECD dataset (most recent)

Source: Treasury and Exchequer



2.4 Operating Deficits

The Budget shows a deterioration in the States' operating balance - income less expenditure and depreciation. The operating balance is a measure of the sustainability of public finances and includes an indicator of depreciation as the cost of 'using' physical capital.

Budget expenditure, net of savings, increases by £103 million, compared to the previous Government Plan. Government income is forecast to increase by £47 million over the same period. As a result, the operating balance has

deteriorated as shown in **Figure 2.6**. **The Panel is concerned that despite higher tax revenues and strong economic growth, the Government's operating balance has deteriorated.**

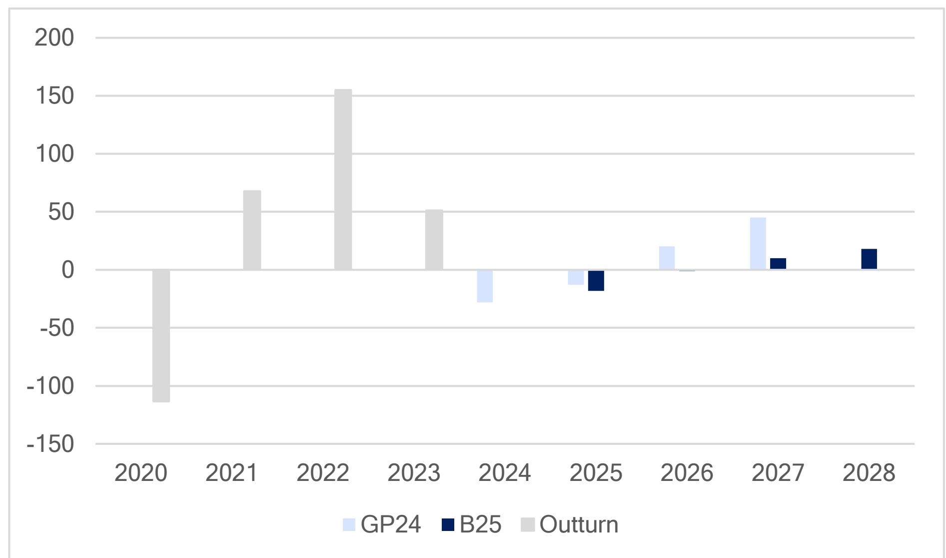
Figure 2.6

Operating balance proposed in Budget 2025-28

£ million (current prices)

Government Plan 2024-2027 vs. Budget 2025-2028 - projections shown in 2024 with forecast shown there after

Source: Treasury and Exchequer



2.4.1 Primary deficits

The 'primary balance' is another measure of the Government's fiscal position. It is the difference between the revenue collected (or forecast) and the amount spent on providing public goods and services. It includes the Government's capital budgets, rather than a depreciation charge, as the cash value of the cost of maintaining its physical assets. Investment returns and borrowing costs, incurred on Governments long-term loans, are excluded from the calculation. Primary surpluses are created when expenditure and the cost of capital spending are fully covered by Government revenues. Conversely, primary deficits mean that Government is needing to rely on reserves or borrowing to fund its planned expenditure. Surpluses are received and deficits are funded through the balance of the Consolidated Fund – Government's current account, which includes its cash reserves.

Government Plan 2024 forecasts a primary deficit in 2025. The Budget increases this primary deficit by £15 million, and forecasts additional surpluses of £17 million across 2026 and 2027 **(Figure 2.7).** The increased surpluses have partly been created by a £20 million reduction to departmental capital investment budget **(Figure 2.8)**.

Increased withdrawals from the Health Insurance Fund (HIF) and temporary adjustments to the Social Security Fund (SSF) grant are being used to finance other areas of expenditure that are not included in the primary deficit. Budget 2025 includes:

- an additional withdrawal of £2 million pa from the HIF to fund additional subsidies for GP appointments. In total, £37 million will be withdrawn from the HIF in 2025-2028.
- £20 million reduction in the ordinary level of annual grant funding transferred from the Consolidated Fund into the SSF over 2025 and 2026

The HIF is expected to be exhausted during the early 2030s and alternative funding will need to be found to continue subsidising the cost of GP appointments. The use of funds to finance additional current spending raises questions about inter-generational fairness.

The Panel is concerned that despite an increase in income the primary deficit has worsened in the first year of the Budget. The Panel believes greater consideration should be given to medium term economic growth and fiscal stability.

Figure 2.7

Revenue income, revenue expenditure and operating and primary balances, Government Plan 2024-2027 vs Budget 2025-2028

£ million (current prices)

Source: Treasury and Exchequer

	2024	2025	2026	2027	2028
General Revenue Income					
GP24	1,191	1,244	1,280	1,327	
B25		1,270	1,297	1,330	1,371
Difference		**46**	**17**	**3**	
Revenue Expenditure					
GP24	1163	1199	1202	1224	
B25		1,230	1,239	1,261	1,294
Difference		**31**	**37**	**37**	
Operating balance					
GP24	-28	-13	20	45	
B25		-18	-1	10	18
Difference		**-5**	**-21**	**-35**	
Primary balance (excluding Our Hospital and NHF)					
GP24	-65	-22	-3	28	
B25		-37	6	47	64
Difference		**-15**	**9**	**19**	

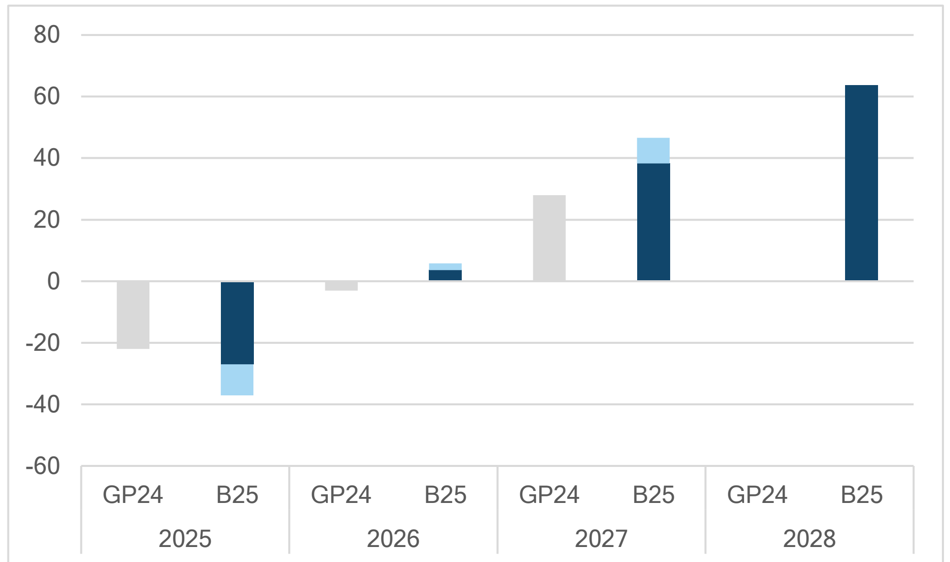
Figure 2.8

Primary balance proposed in Budget 2025-28

£ million (current prices)

The primary balance shows a deficit in 2025 with surpluses in further years. The light blue shows how the capital expenditure budget has been cut, improving the primary balance indicated by the position of the dark blue

Source: Treasury and Exchequer



2.5 Consolidated Fund

The Consolidated Fund is the Government's current account, in which all monies are received and spent. Under the Jersey Public Finance Law 2019, the government is unable to lodge a Budget (or previously Government Plan) in which the Consolidated Fund is forecast to have a negative balance. Although the Budget forecasts that the Consolidated Fund's balance will improve in 2024 and 2025, the Fund's closing balance will only be £1 million in 2027 and 2028 due to the proposed increases in expenditure and the primary deficit forecast for 2025 **(Figure 2.9).**

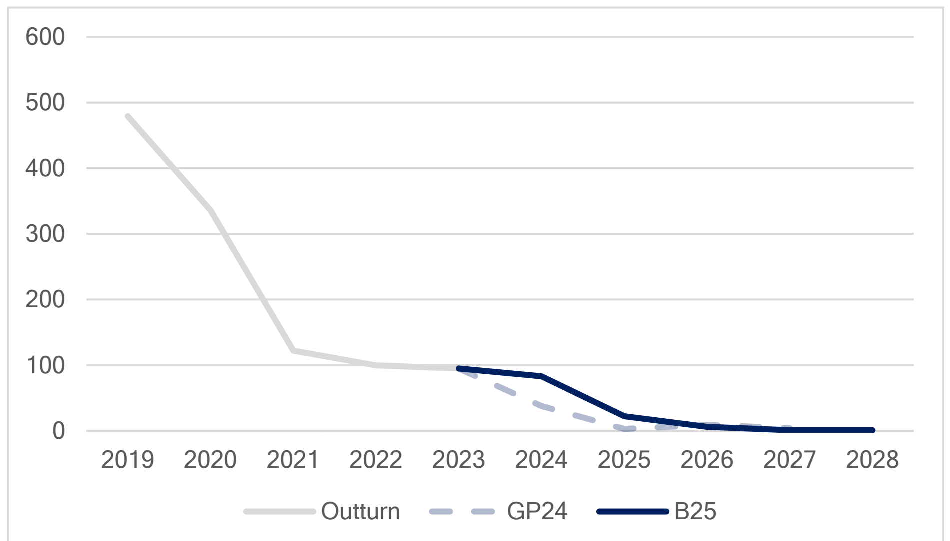
Figure 2.9

Consolidated Fund balance

£ million

Government Plan 2024-2027 vs. Budget 2025-2028

Source: Treasury and Exchequer



2.7 Capital Expenditure

The Budget allocates £308 million to capital budgets over 2025 – 2028, not including the New Hospital Facilities capital project. This represents a reduction of around £21 million compared to Government Plan 2024 for years 2025 -2027 (Figure 2.10). The Budget describes this capital programme as being more 'deliverable', noting that previous capital budgets had been underspent. Budget 2025 also includes plans to deliver Phase 1 of the New Hospital Facilities - a major capital investment of up to £710m. **The Panel welcomes the setting of capital budgets at deliverable levels. However, the Panel recommends that any reductions in capital budget are invested in the Stabilisation Fund and not used for additional current expenditure. Further, the Panel notes that to meet the challenges set out in the Future Economy Programme, Jersey will need higher levels of well-directed public investment that are focused on enabling economic growth.**

Figure 2.10

Capital Expenditure Budgets

£ million

Proposed capital spending from the Consolidated Fund (current account) – not including the NHF project

*Chart amendment made 25/09/2024

Source: Treasury and Exchequer

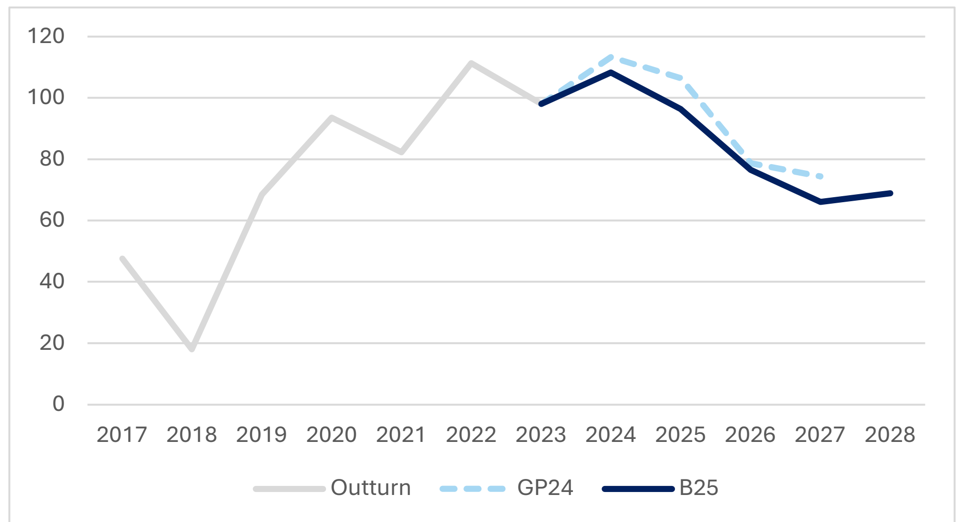


Figure 2.11 shows that Jersey's Gross Fixed Capital Formation ('GCFC') – a measure of aggregate capital investment – as a percentage of GDP is significantly lower than international comparisons. Under-investment will negatively affect the economy's ability to deal with long-run challenges like an ageing population and declining productivity. Investment in the New Healthcare Facilities will increase measured investment and will close the 'investment gap' with other economies. If Jersey is to meet the twin challenges of an ageing population and low productivity, the pace and scale of investment will need to increase. Specifically, higher levels of well-directed capital spend prioritised on projects that increase productive capacity and support long-run

growth will be needed. **In light of this, the Panel recommends that the Government considers how to address the existing capability and capacity constraints.**

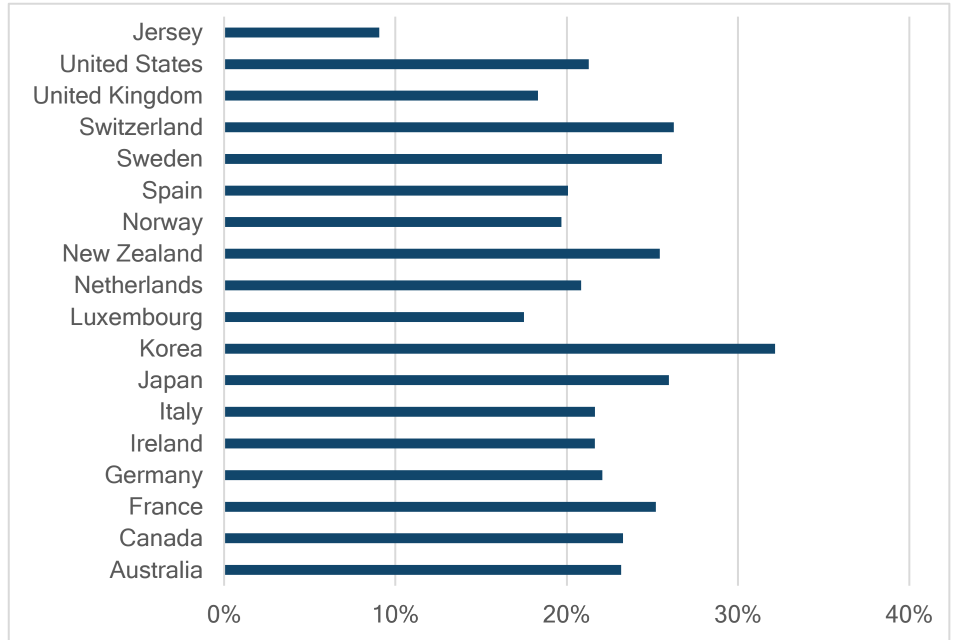
Figure 2.11

Investment GFCF as a proportion of GDP 2022

2022 prices

Jersey's measure of aggregate capital investment compared to selected OECD economies (using most recent available data)

Source: Treasury and Exchequer



The Budget increases capital spending on IT (+ £19 million) and decreases capital spending on estates and infrastructure (- £42 million) **(Figure 2.12)**

The largest individual areas of spending / projects in the Budget include:

- Mont a' L'Abbe Secondary
- New School and Educational Developments
- Upgrades to CYPES estates
- Major Refurbishments and upgrades
- Cyber Programme 2.0
- IT Major upgrades and replacement
- Revenue Transformation Programme (Phase 4)

The majority of these have been designated as 'major projects' and therefore will span multiple years.

Figure 2.12

Capital Spending by Category

£ million

Source: Treasury and Exchequer

Capital programme area	2025	2026	2027	2028	Total 2025-2028
Feasibility	1	1	1	-	3
Estates	28	18	26	33	106
Infrastructure	30	30	20	24	103
Information Technology	21	16	10	1	47
Replacement Assets and Minor Capital	13	11	11	11	45
COCF funded projects	3				3
Total	**96**	**76**	**66**	**69**	**307**

2.8 Future Income: Pillar Two

In 2024, Jersey announced its plan to introduce the Organisation for Economic Co-operation and Development ('OECD') Pillar Two global, minimum tax framework for large multinational groups. Starting from 2025 Jersey will introduce a new minimum tax rate of 15% on all corporations within scope of Pillar Two. The majority of those affected by Pillar Two are currently within either the 0% or 10% Corporate Income Tax regimes and so the introduction of Pillar Two can be expected to generate additional tax revenue.

The Budget sets out the base case forecast for additional Corporate Income Tax payments relating to Pillar Two. This is the forecast minimum recurring annual additional tax revenue of £52-£54 million per year. This tax revenue is additional to the main tax forecast and the Budget proposes it should be reserved for investment and for rebuilding the island's reserves rather than on current expenditure. The Budget sets out proposals for how it will be allocated across multiple spending and investment priorities **(Figure 2.13)**:

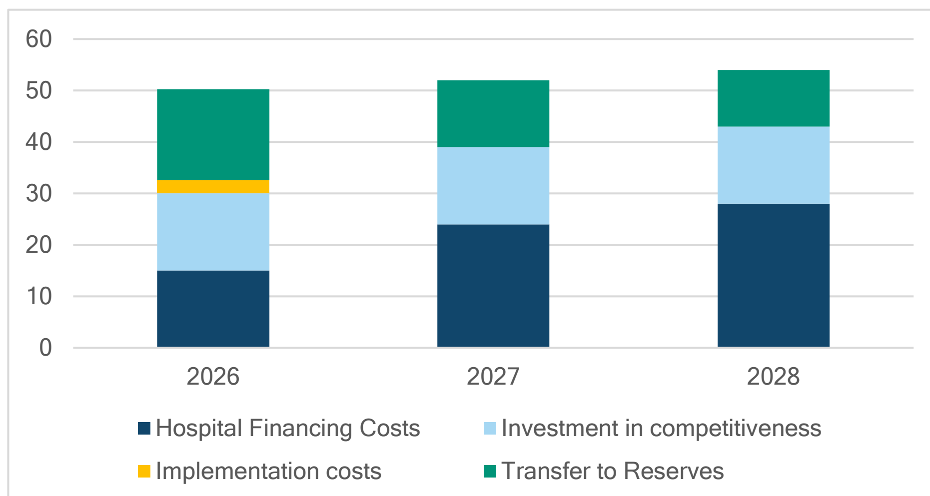
- Offset NHF finance costs (otherwise funded by drawing down the Strategic Reserve)
- Re-invest into the finance sector (maintain competitiveness)
- Transfer to Reserves
- Implementation costs

Figure 2.13

Spending of Pillar Two income

£ million

Source: Treasury and Exchequer



In the event that Pillar Two revenues exceed the base case forecast, the Budget proposes a funding hierarchy to inform the allocation of any additional tax receipts:

1. Offset NHF capital costs funded by drawing down the Strategic reserve
2. Further replenish Stabilisation Fund
3. Reduce NHF borrowing
4. Transfers into the Strategic Reserve

The Panel strongly supports the allocation of forecast Pillar Two tax revenue to investment and to the Reserves along with the prudent approach to forecasting this income, **The Panel recommends a formal commitment to ringfence any Pillar Two income in excess of the base case forecast for investment in the Strategic Reserve or Stabilisation Fund.**

2.9 New Healthcare Facilities

The Budget includes the proposition for the New Healthcare Facilities (NHF) Phase 1 financing strategy. The NHF project is estimated to cost £800 million, of which £90 million has already been accounted for. Budget 2025 proposes a blended financing strategy using borrowing, revenues and the Strategic Reserve:

- **2024-2026:** £523 million of public borrowing, including £142 million of existing borrowing approvals, with up to £500 million made available through a Revolving Credit Facility

- **2027-2028:** £277 million funded from the Strategic Reserve or potentially funded through Pillar Two receipts if these exceed the baseline forecast.
- Interest costs totalling £76 million will be met by the base case Pillar Two forecast and the Strategic Reserve will only be used to fund the £9 million financing costs in 2025.

2.9.1 Debt

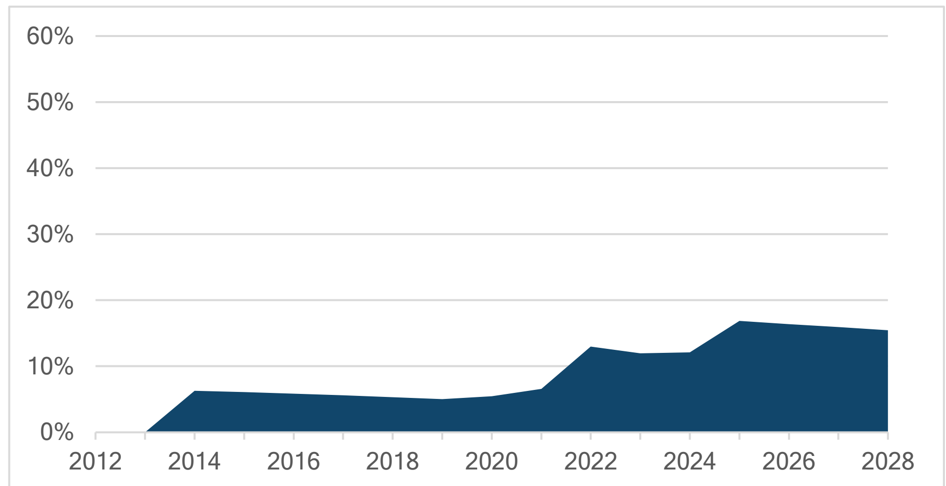
The borrowing proposals included in the NHF financing strategy will increase the level of Jersey's public debt by £381 million. The gross debt-to-GDP ratio will reach 17% in 2025. Whilst low compared to many countries, this represents a significant increase in recent years – the ratio was 5% in 2019 and 12% in 2024 **(Figure 2.14).** While using the Strategic Reserves reduces the borrowing requirement and protects the government from further, expensive interest costs, it also reduces the ability of the Strategic Reserve to support or protect Jersey's economy should a crisis occur.

Figure 2.14

Debt as a percentage of GDP

£ million (current prices)

Source: Treasury and Exchequer



2.10 Reserves

Reserves are an essential part of the government's balance sheet. The total value of the government's 7 major reserves **(Figure 2.15)** is forecast to grow to £4,429 million by 2027 (56% of GDP), before seeing a net decrease of £22 million in 2028.

Figure 2.15

Government of Jersey's major reserves

£ million (current prices)

Source: Treasury and Exchequer

	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
	Actuals					Estimate				
Consolidated Fund	479	36	122	100	95	83	22	6	1	1
Strategic Reserve *(as a % of GVA)*	906 (18%)	968 (21%)	1,032 (20%)	992 (17%)	1,090 (16%)	1,1124 (16%)	1,449 (20%)	1,506 (20%)	1,516 (19%)	1,349 (17%)
Stabilisation Fund	50	1	1	1	1	1	1	1	1	1
Social Security Reserve Fund	1,983	2,093	2,264	2,031	2,179	2,320	2,429	2,543	2,671	2,810
Social Security Fund	92	76	66	70	89	86	88	90	100	112
Health Insurance Fund	108	108	100	105	112	104	94	85	76	67
Long Term Care Fund	26	37	41	49	45	56	58	61	64	67
Total	**3,645**	**3,608**	**3,626**	**3,347**	**3,611**	**3,774**	**4,141**	**4,292**	**4,429**	**4,407**
Total as % of GVA	***73%***	***79%***	***71%***	***57%***	***53%***	***53%***	***56%***	***56%***	***56%***	***54%***

2.10.1 Strategic Reserve

The Panel continues to recommend that the value of the Strategic Reserve should be equal to between 30-60% of GVA to ensure that sufficient resources are available to the Government in the occurrence of a major economic crisis. The Budget has taken steps to increase the Fund's value, but even with these commitments, the Strategic Reserve still falls short of the FPP target **(Figure 2.16)**. In cash terms, the Strategic Reserve is replenished more slowly which is a concern should a major crisis were to occur in the near future. Furthermore, the proposed NHF financing strategy requires withdrawals of £277 million (19% of the 2025 value) from the Strategic Reserve.

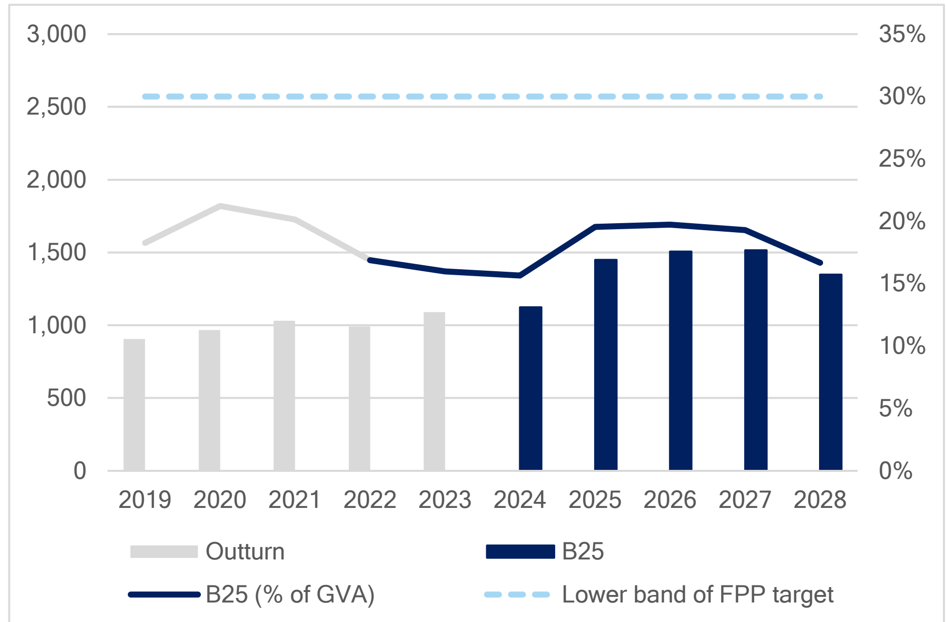
Figure 2.16

Strategic Reserve balance

£ million (current prices)

Bars show total value of the Strategic reserve (LHS), the line shows the value as a percentage of GVA (RHS), the dashed line shows the lower bound of the FPP recommended value 30-60% of GVA (RHS)

Source: Treasury and Exchequer



The Panel welcomes the transfer of the Prior Year Basis ('PYB') taxation debt into the Strategic Reserve. This asset boosts the value of the Strategic Reserve in accounting terms by £280 million. However, the Strategic Reserve is only expected to receive £12.5 million in repayments annually. This means that it will be over twenty years until the Strategic Reserve's cash balance has the total £280 million available to respond to a major shock to the island's economy. A more accurate presentation of the resilience afforded by the Strategic Reserve is set out in **Figure 2.17** which shows the 'liquidity' value of the Strategic Reserve or the cash it has available to respond to shocks. This shows that the cash value of the Strategic Reserve is decreasing across the Budget period. **The transfer of PYB taxation debt, in line with the Panel's previous recommendation, is welcomed. Nonetheless, the Panel remains concerned that the Strategic Reserve's level of liquidity may not be sufficient to provide the government with immediate cash injections if a major crisis was to occur in the short or medium-term. The Panel reiterates the importance of using Pillar Two income to support the value of the Reserve.**

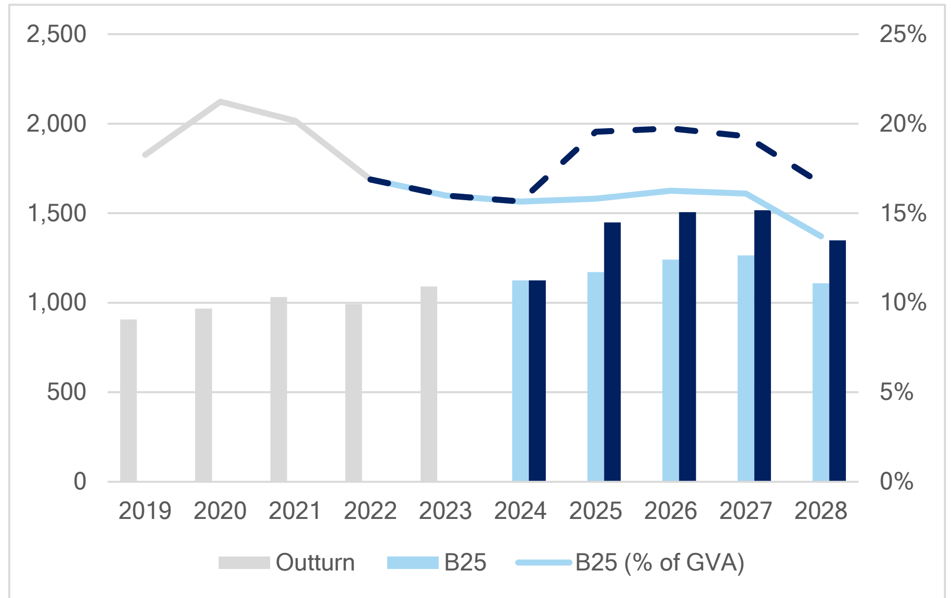
Figure 2.17

Strategic Reserve balance, only recognising cash value of PYB asset

£ million (current prices)

The light blue indicates that the liquidity value of the Strategic Reserve is decreasing. The dark blue and dashed line is the asset value shown in the previous graph

Source: Treasury and Exchequer



2.10.2 Stabilisation Fund

Stabilisation funds are particularly important in economies like Jersey's that lack both the monetary policy levers or the powerful tax and benefit regimes that can act to help stabilise the economy in a downturn.

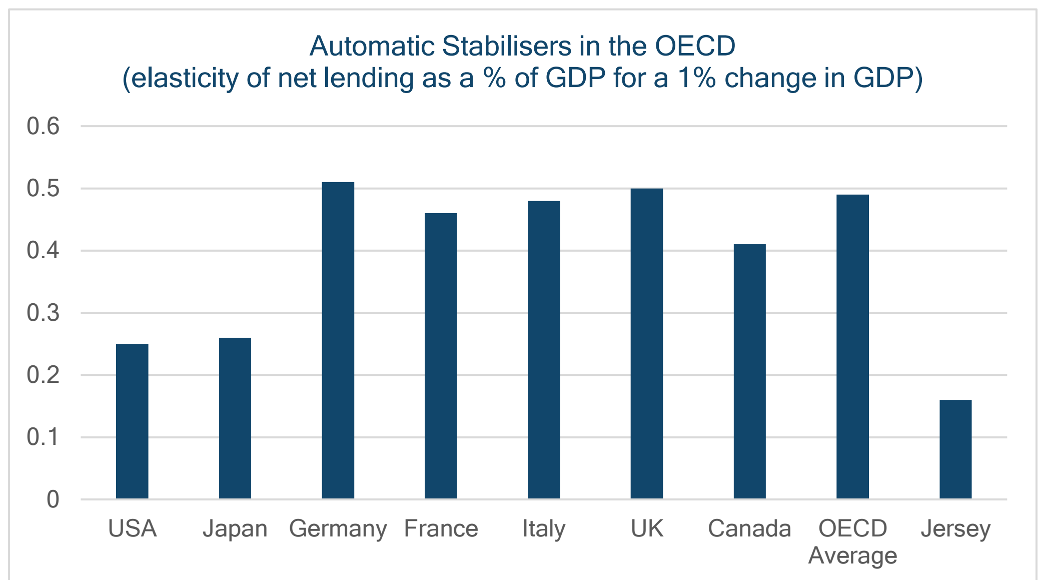
The Stabilisation Fund is effectively exhausted at present. The recent period of strong tax revenue receipts offered a major opportunity to rebuild the Fund as recommended in the Panel's previous report. The panel calculates that £50-£80 million could have been contributed to the Stabilisation Fund since the start of 2021, when the economy began to grow strongly. Investing this income, as recommended by the Panel in its previous report, into the fund would have reduced overheating in Jersey's economy and would have created a reserve capable of supporting Government revenues in case of a period of economic downturn.

The Panel strongly recommends that any current year surpluses or underspends are immediately committed to the Stabilisation Fund, and that the Government commits to investing a proportion of upside Pillar Two revenues into this fund.

CYCLICAL FISCAL POLICY AND ECONOMIC STABILITY

Jersey's Boom/Bust Cycle and the Stabilisation Fund

A common feature of small economies like Jersey is that they tend to go through more extreme boom-bust cycles than their larger compatriots. This is mainly due to the fact that small economies, almost inevitability, end up with a single dominant export industry rather than a diversified industrial base. Added to this, Jersey's fixed exchange rate, whilst avoiding the FX rollercoaster experienced by other small economies with their own floating currency (such as Iceland and the Seychelles), means that monetary policy (changing interest rates) cannot be used to help lean against booms and busts.

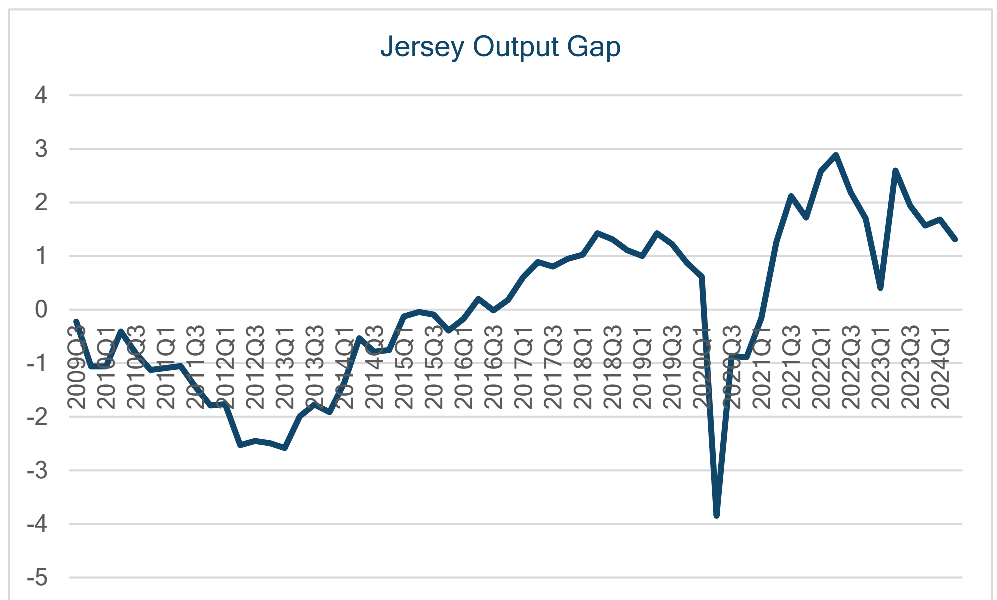


[1] *Estimated using the approach outlined in Den Noord (2000) OECD working paper 230*

Given that background, there is a strong case for Jersey in directing fiscal policy to help offset the cycle - with the government spending more than it receives in taxes in a recession and vice versa in booms. In practice some of this should happen mechanically through a system called automatic stabilisers. In a boom, when tax revenue is strong and spending on things like unemployment benefit tends to fall, the government should automatically find itself spending less than it receives in taxes and vice versa for a recession. Background work by the FPP[1] has estimated the strength of these automatic stabilisers in Jersey, they are weaker than in most countries, partly due to the small government, but should operate such that for every 1% of boom (above trend growth) in Jersey the fiscal position should improve by about 0.16% of GVA.

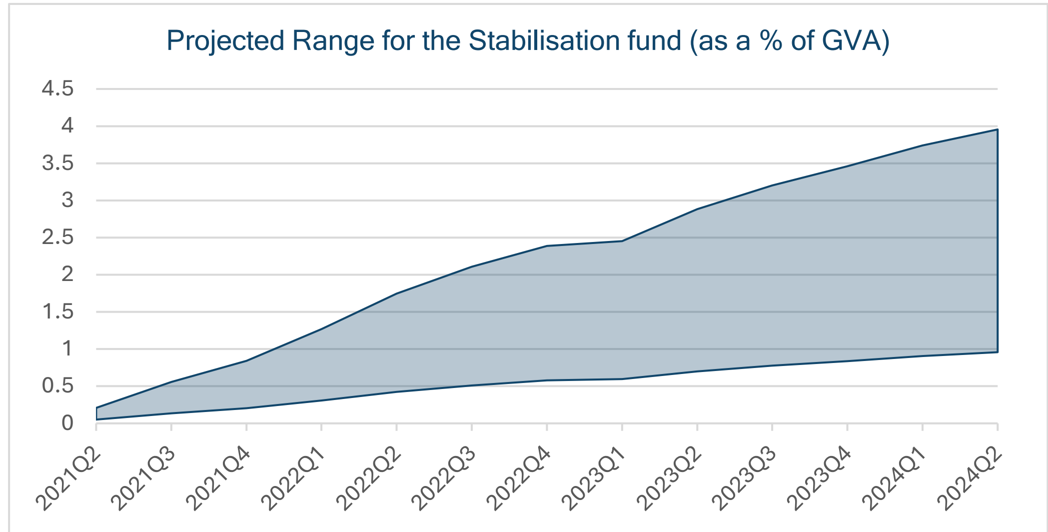
The Economic Cycle in Jersey

Given that automatic stabilisers are quite weak in Jersey, there is a strong argument for the government leaning against the boom/bust cycle more actively (deliberately running a tight budget in booms and a loose one in recessions) but to do that it is important to keep track of the cycle itself. The standard approach to looking at the cycle is through a concept called the output gap, which is a measure that is above zero when the economy is in a boom and below zero when in a bust. The chart below shows recent developments in Jersey's output gap (estimated using data from the BTS survey, unemployment and vacancies) and show that Jersey is coming toward the end of a multi-year boom.



It's important to remember a boom like the one Jersey has recently experienced does not mean everyone feels richer it simply means that the productive resources, such as the available labour force, of the economy are stretched so that further spending (including government spending) will simply result in off-island spending and/or inflation.

Against the background of this recent boom, Jersey's government finances are in a surprisingly weak state and the Stabilisation Fund (the fund where excess revenues from booms is kept in order to be available at the next bust) is effectively at zero when even the simple operation of automatic stabilisers would suggest a balance of about 1% of GVA, or £60 million, should have been accumulated. This figure represents a minimum of what should already have been accumulated as it is the amount that should have gone to the Stabilisation Fund if the objective of the government was simply to avoid pro-cyclical fiscal policy (policy that makes the boom/bust cycle worse). In practice, in a country like Jersey fiscal policy should lean against the cycle and try to dampen to boom bust cycle. So, for example, if Jersey has set policy so as to offset half the excess demand in the economy the fund should have accumulated £250 million giving a large war chest to offset a future cyclical bust.



2.10.3 Health-related Funds

Budget 2025 increases the rate at which both the Health Insurance and the Long-Term Care Funds are drawn **(Figure 2.18).** The value of the Health Insurance Fund is forecast to be worth less than £70 million at the end of the Budget period – equivalent to one year of its expected expenditure level.

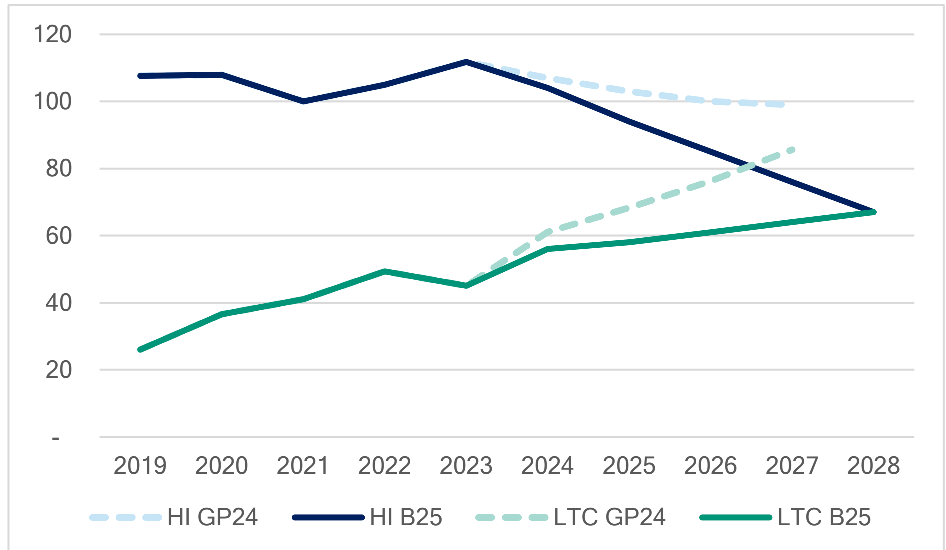
Figure 2.18

Health Insurance and Long-term Care Fund

£ million

Government Plan 2024-2027 vs the Budget 2025-2028

Source: Treasury and Exchequer



Although the value of the Long-Term Care Fund is still expected to increase over the Budget period, the growth trajectory is considerably lower than the Government Plan 2024 forecast and will be under government's close review in 2025.**The Health Insurance Fund will be severely depleted by the end of the**

Budget period and is expected to be exhausted by early 2030's. As the HIF is currently being used to fund some health costs, its exhaustion will create a funding gap and raises questions about the future of the HIF. The Panel recommends this is considered soon.

2.10.4 Social Security Funds and Living Wage

The Social Security Fund and the Social Security Reserve Fund are the Government reserves responsible for the provision of old-age state pensions. In the Budget, the closing balance of the Social Security Fund, which is the current account used for making benefit payments, will be £29 million lower in 2027 when compared to Government Plan 2024. This is a result of the government's decision to reduce the ordinary level of grant funding made from the Consolidated Fund by £10 million in 2025 and 2026 to fund the Living wage business support package. **The Panel notes that in cutting the grant to the Social Security Fund, the full scale of the proposed increase in current expenditure is under-stated and that the balance of the Social Security Fund is reduced.**

In 2027, the Social Security Reserve Fund's closing balance is forecast to be £151 million higher when compared to the previous Government Plan. Protected to help finance the pension cost of Jersey's ageing population, the Social Security Reserve Fund is the Government's largest individual fund with forecast value of £2,810 million in 2028. Jersey's ageing population will create significant pressures for the island's public finances, as such, **The Panel recommends a review of this fund be undertaken to better understand the extent to which the fund is sufficient in meeting expected future pension liabilities.**

2.12 Balance Sheet

The balance sheet shows the net value of government's total assets, including capital, reserves, and liabilities which measure borrowing and other long-term liabilities. The value of the government's physical and financial assets is forecast to increase by £1,216 million between 2024 and 2028, but this will be offset by the £505 million addition for non-current liabilities - the NHF borrowing scheme. Although the government's net asset nominal value is set to increase, as a percentage of GDP it is forecast to decrease from 116% in 2024 to 111% in 2028 **(Figure 2.19)**.

In 2019, net asset value was equivalent to 152% of GVA (calculated as GDP from 2021 onwards). As in most advanced economies, the pandemic and cost

of living crisis has eroded the net value of states assets. However, by using reserves and capital budgets to support the balance of the current account and fund current expenditure, Government has been unable to improve net asset value as a proportion of GDP despite strong recent tax revenues. Furthermore, increasing States borrowings has led to the further deterioration in net asset value over this budget period.

Figure 2.19

Government of Jersey's Net asset value in Budget 2025-2028

Net asset value includes that of government and its subsidiaries. Bars show nominal value in £ billion (LHS), line shows value as a proportion of GDP (RHS).

Source: Treasury and Exchequer