

# Jersey Government Plan 2021-24 Covid-19 Recovery Planning Response

Economic and International Affairs Panel

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**Jeffrey Matsu**  
Chief Economist, CIPFA  
[jeffrey.matsu@cipfa.org](mailto:jeffrey.matsu@cipfa.org)

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# Preface

In August 2020, the States of Jersey commissioned CIPFA Business - Finance Advisory (the commercial arm of the Chartered Institute of Public Finance and Accountancy) to support the work of the Economic and International Affairs Panel in the Review of the Jersey Government's Covid-19 Response and Recovery approach. This report seeks to support the Panel's work by commenting upon the latest draft version of the Government Plan 2021-24.

## 1. Introduction

The confluence of social, economic and political uncertainties has made 2020 a turbulent year. According to the World Bank, 93% of countries are estimated to be in recession.<sup>1</sup> This follows the decade since the global financial crisis (GFC) where many advanced economies faced a persistence of low growth, low inflation and low productivity. Although recent news of clinical success in vaccine development offers hope, a second wave of Covid-19 infections has required renewed national lockdowns in countries such as the UK, France and Germany. Complacency is a particular risk at this stage of the crisis and will require leaders to weigh the costs and benefits of future responses.

For a jurisdiction the size of Jersey with a population of 107,800, the Government Plan 2021-24 offers a structured and relatively comprehensive road map.<sup>2</sup> There is clarity in vision and purpose that aligns current realities with future ambitions. Sustainability resonates as a theme throughout the document, underpinned by a commitment to sound public financial management. Indeed, the fiscal framework recognises the need to strike a balance between the crisis response today and resourcing to fulfil longer-term commitments in areas such as healthcare and retirement.

Equally, there is a palpable sense of fiscal conservatism within the Plan that may hinder its ability to secure a stronger recovery for the benefit of all islanders. Given the uneven impacts that Covid-19 has had across the economy, inequalities will grow across such dimensions as age, gender, race and income. More targeted fiscal responses can help to alleviate such pressures before they lead to structural effects on the demographic profile of Jersey that may be costly to unwind. High risk events such as subsequent waves of Covid-19 infections or a no-deal Brexit would warrant more explicit planning beyond the scaling up of previous interventions.

Mechanisms to improve communication across government, businesses, industry and civil society have the potential to mobilise support for this Plan. Data collected through channels such as the Jersey Opinion and Lifestyle Survey (JOLS) and Government Plan 2021-24

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<sup>1</sup> <https://www.worldbank.org/en/news/feature/2020/06/08/the-global-economic-outlook-during-the-Covid-19-pandemic-a-changed-world>

<sup>2</sup> <https://www.gov.je/News/2020/Pages/Population-Estimate-2019.aspx>

Surveys provide a useful steer on policy direction and can strengthen much needed civic engagement. With voter turnout in Jersey lower than in all OECD countries, the government might consider running such surveys more frequently with a view to better gauging changes in public sentiment. Meanwhile, digitisation can improve the reach of government services at often reduced costs, but performance must be measured to ensure that it does not disadvantage those with limited access.

## 2. Economy

As the global pandemic approaches its anniversary, high levels of continued uncertainty have made economic forecasting prone to sizeable revision. In its latest World Economic Outlook<sup>3</sup>, the IMF estimates global GDP to fall by 4.4% this year compared to the -3.3% it thought in April. The UK was downgraded even further from -6.5% to -9.8% which in normal times would be considered extraordinary. To reflect a range of plausible outcomes, downside and upside scenarios show the level of global GDP in 2025 as 1.5% below and 2% above the baseline, respectively. Given the significant epidemiological unknowns and therapeutic challenges that remain, risks are viewed to the downside.

Economic projections undertaken by Jersey's Fiscal Policy Panel (FPP) are also highly variable.<sup>4</sup> Real gross value added (GVA) was expected in its March assessment to fall by 6.3% this year but has since been revised to -7.6%. Similarly, the quarterly growth profile assumed as V-shaped will now be noticeably less so. This was magnified by a large underestimation of real GVA for 2019 – the outturn of 2.1% was significantly better than the 0.6% annual growth the FPP envisaged as recently as its August forecast update. By the end of 2023, economic output in Jersey would still be about five percent less than it was compared to its pre-crisis peak.

Although the FPP foresees economic activity next year rebounding to 3%, with above trend growth in 2022 and 2023, the outlook remains fragile. The likelihood of scarring from a deep recession is high, particularly if subsequent waves of Covid-19 infection result in a prolonged period of global malaise and introspection. Reduced tourism would hit already weakened demand in Jersey's travel and hospitality sectors. A correction in financial markets that hitherto have remained buoyant could send shock waves across an economy heavily reliant on their performance. Indeed, the low interest rate environment that has fuelled investment into alternative assets, and which is expected to sustain the public finances going forward, may soon enough become a significant headwind.

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<sup>3</sup> <https://www.imf.org/en/Publications/WEO/Issues/2020/09/30/world-economic-outlook-october-2020>

<sup>4</sup>

<https://www.gov.je/Government/Departments/OfficeChiefExecutive/OfficeChiefExecutivesSections/Pages/FiscalPolicyPanel.aspx>

While monetary policy in the UK is expected to remain highly accommodative with the market-implied path for Bank Rate going negative in 2021 and 2022, unexpected inflation may require the Bank of England to change tack.<sup>5</sup> If the UK is unable to agree to a free trade agreement with the European Union by the end of this year, a “hard Brexit” could lead to a substantial weakening of the British pound that results in higher imported prices. Additional inflationary pressures could appear if the much anticipated Covid-19 vaccine proves successful, marking a decisive end to the pandemic and leading to a resurgence in domestic demand. Moreover, recent research by Charles Goodhart, emeritus professor at the London School of Economics, argues that ageing societies and a retreat from globalisation have set in motion structural changes that will give way to a revival in inflation.<sup>6</sup>

The government of Jersey could be better positioned to respond to the challenges that the crystallisation of such risks might present by embedding contingency plans more explicitly into the Government Plan. A fiscal strategy that disproportionately protects reserves in favour of increased borrowing exposes the public finances to market volatility which, to date, has remained relatively subdued. There may also be an overreliance on the FPP’s central scenario without enough planning for the effects of a stronger negative impulse from non-domestic factors as noted above.

### 3. Fiscal framework

One of the lessons learned from the post-GFC experience has been not to withdraw policy support prematurely. During the event, the outsized monetary response in many advanced economies was followed by calls for fiscal consolidation before a stable economic recovery had been secured. The effects were particularly acute in countries such as the UK which chose to slash funding for public services while pursuing ultra-accommodative monetary policy in the form of a sustained low Bank Rate and additional quantitative easing. The cumulative effect was a lost decade lacking the economic vigour necessary to handle the ravages of the next crisis.

In response to Covid-19, multilateral organisations have adopted a far more holistic narrative that recognises the importance of rapid and generous counter-cyclical public spending. According to the IMF, governments around the world have provided an exceptional \$12 trillion in fiscal support since the start of the pandemic to address cumulative economic losses which are projected to grow from \$11 trillion to \$28 trillion by 2025.<sup>7</sup> Across the G7, these budgetary measures have averaged 8% of GDP compared to 3.2% in 2009. The surge in public and private sector debt carries unprecedented risks which will require agility in navigating as economies move through different phases of the pandemic.

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<sup>5</sup> <https://www.bankofengland.co.uk/monetary-policy-report/2020/november-2020>

<sup>6</sup> <https://pagesofhackney.co.uk/webshop/product/the-great-demographic-reversal-charles-goodhart-manoj-pradhan/>

<sup>7</sup> <https://www.imf.org/en/Publications/FM/Issues/2020/09/30/october-2020-fiscal-monitor>

Against this rapidly evolving global backdrop, Jersey has a unique opportunity to reallocate both risks and opportunities across its economy. The Government Plan acknowledges that “multiple approaches will be required to balance government finances, including a wide range of fiscal measures, borrowing strategies, economic stimulus, treatment of funds and the delivery of savings and efficiencies.” Measures include £3.5 million of revenue generation starting next year, £700 million of borrowing in 2022 and nearly £400 million in capital expenditure over the planning period. Underpinning the island’s fiscal framework remains a commitment to increasing the Strategic Reserve and public sector net worth, running a primary structural current balance or surplus over time, and borrowing only to finance investment or refinance liabilities. These actions are expected to culminate in a balanced budget by 2024.

The government’s focus on financial sustainability when the global pandemic has not yet peaked suggests that more can be done to prepare for the unexpected. Covid-related costs will amount to 5% of the island’s GVA this year which is similar to that of France but smaller than the 8% spend in the UK.<sup>8</sup> This falls to 2% in 2021 and then to zero for the remaining three years of the Plan despite the fact that a vaccination programme is unlikely to be initiated until sometime in the spring – with winter and the festive season yet to begin. The fragility of the economic outlook, financial markets and Brexit negotiations may result in concurrent funding pressures that could be partially alleviated by securing an earlier and more robust recovery today.

Although the government seeks to achieve a balanced budget by the end of the four-year planning period, it is unclear why a surplus is needed as early as 2023 given the attendant risks. The financial principles that guide decision-making within the Plan call for “long-term financial sustainability with balanced budgets in the medium term” which suggests that the latter may be just three years. There is a reluctance to mobilise funds set aside in the Strategic Reserve despite its stated purpose being “to protect the island’s economy from severe structural decline... such as from major natural disaster.” According to Jersey’s FPP Annual Report 2020, “the economy should not be expected to return to its pre-pandemic path and therefore any ongoing increase in costs in later years should be considered permanent/structural impacts.”<sup>9</sup> Yet the reserves are maintained at 18-19% of GVA with an ambitious target of reaching 30% over the long-term, however that is defined.

Similarly, great importance is placed on the counter-cyclical support provided by the Stabilisation Fund but less clear is whether the £50 million would be enough for future crises that do not meet the criteria to access the Strategic Reserve. Transferring funds from one programme to bridge a gap in another may create immediate fiscal space but risks shifting pressure elsewhere within the system and across time. In doing so, the Plan widens the scope for unintended consequences if revenue or spending projections do not go to plan. As some of these effects can take years to manifest, extra vigilance will be required.

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<sup>8</sup> <https://www.bruegel.org/publications/datasets/Covid-national-dataset/>

<sup>9</sup>

<https://www.gov.je/SiteCollectionDocuments/Government%20and%20administration/ID%20FPP%20Annual%20Report%20October%202020.pdf>

The government should urgently prioritise a review of the funding arrangements for the Social Security Fund as it is not obvious why a drawdown on the Social Security Reserve is the preferred option given the fixed nature of future payment streams. Indeed, the volatility in the Government of Jersey Group forecast over 2021-24 underscores the high degree of uncertainty inherent in projecting investment returns. Coupled with the island's ageing population demographics, this could have significant repercussions on the Fund's ability to sustain itself in future years.

The preference to shore up reserves and increase borrowing to meet the financial challenges caused by the pandemic is premised on Jersey's low debt levels, high credit rating and the tenuous assumption that "the cost of debt will be far lower than the long term returns on our reserves." Active diversification in the risk profile of investments can offset some of the increased leverage on the government balance sheet. Fuller disclosure of such strategies within the Government Plan would aid the assessment of total risk exposure. Given the heightened degree of uncertainty during the planning period, the government should also be adequately prepared for an environment where interest rates rise without a corresponding increase in economic growth.

## 4. Rebalancing and inequalities

Performance measurement based on outcomes will be key to ensuring that stimulus-related projects deliver efficiency and value for money. Traditional cost benefit analyses in determining the allocation of public funding may prove insufficient to influencing the range of social and environmental challenges presented in the Government Plan's Common Strategic Policy (CSP) Priorities. Jersey has an opportunity to consider innovations such as outcomes-based contracting, impact bonds and social impact investing to deliver upon these commitments.

While preventative measures are a good first line of defence – but often the first to go when resources become constrained – tackling complex social issues such as homelessness and chronic unemployment will require access to, and the better understanding of, community data. Utilising algorithms that run large datasets against demographic and other risk factors has the potential to guide better decision-making from how to distribute benefits to rapidly identifying citizens whose support needs may escalate due to the pandemic.<sup>10</sup> Global initiatives such as the International Network for Data on Impact and Government Outcomes (INDIGO) can help Jersey learn from the experiences of other jurisdictions as well.<sup>11</sup>

Covid-19 has magnified social and economic disparities and divergences that were long in the making. In the UK, for instance, a decade of austerity cut public services so severely that

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<sup>10</sup> <https://www.cipfa.org/services/data-analytics/Covid19-oneview-service>

<sup>11</sup> <https://golab.bsg.ox.ac.uk/toolkit/INDIGO-Intro2020/>

the landscape has been left deeply scarred. Discretionary spending in areas such as housing, planning and transport, not to mention youth centres, parks and libraries, was hardest hit. Even mandatory services in health, social care, criminal justice and schools experienced reductions in quality and scale that will be difficult to reverse. Since 2009, cuts in central government funding have led to English local authorities spending 17% less on public services. The distributional consequences have been remarkable with per capita spending reduced by 31% in the most deprived areas compared to 16% in the least deprived, according to data from the Institute for Fiscal Studies (IFS).<sup>12</sup>

Wider inequalities across age, gender and race will warrant more robust policy frameworks in Jersey as well. While young people may be less susceptible to the Covid-19 virus, they have shouldered the weight of job losses and reduced job prospects, not to mention disruptions in their education and the prospect of higher taxes that will endure for years to come. According to the Jersey Opinion and Lifestyle Survey (JOLS), 43% of respondents under the age of 35 reported high levels of anxiety or stress since the start of the pandemic – more than double the average rate of cohorts aged 55 and over.<sup>13</sup> A worrying 60% of adults also cited COVID-19 as having a negative impact on their children’s educational progress.

Women too are more likely to work in sectors such as retail and hospitality that have shut down or are disproportionately represented in lower paid frontline key worker roles. More than a quarter of working adults who responded to the JOLS reported an increase in hours worked while 21% found themselves having to work around childcare or home schooling. Meanwhile, recent analysis from the IFS’s Deaton Review evidences how ethnic minorities are now more economically vulnerable due to underlying factors related to age, geography, income and health. In the UK, for example, only a third of Bangladeshi, black Caribbean and black African households have enough savings to cover a month’s income compared to 60% for the rest of the population.<sup>14</sup>

In addressing the CSP Priorities, a more thorough appraisal of existing data can help the Jersey government direct funds where inequalities are the greatest. Outcomes relating to education, health, housing and income are highly correlated with an individual’s personal background yet many of these indicators are either absent in surveys such as the JOLS or not reported in a useful way in the official statistics (e.g. “place of birth” in the national census). By improving the kinds of statistics that are collected, particularly along the dimensions of race and ethnicity, Jersey can enable the framework for a fairer society that would enhance resident well-being and the island’s overall identity.

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<sup>12</sup> <https://www.ifs.org.uk/uploads/R-174-COVID-19%20and%20English-council-funding-how-are-budgets-being-hit-in-2020%E2%80%9321.pdf>

<sup>13</sup>

<https://www.gov.je/SiteCollectionDocuments/Government%20and%20administration/R%20Opinions%20and%20Lifestyle%20Survey%202020%20Report%2020200903%20SJ.pdf>

<sup>14</sup> <https://www.ifs.org.uk/inequality/>



## 5. Next steps

Continued near-term support that is timely, targeted and temporary is warranted given the severity of the recession and the considerable risks that remain to the outlook. Survey-based evidence from the JOLS and Business Tendency Survey (BTS) show signs of stress and fatigue across the island as the pandemic soon approaches its anniversary. Although only 8% more of respondents to the BTS reported a decrease rather than increase in business activity in September (compared to -60% the previous quarter), the net balances on profitability and business optimism remain in deeply negative territory at -33% and -23%, respectively.<sup>15</sup> In its effort to stimulate local activity in what should be one of the busiest times for high street retailers, the government might consider increasing the size and frequency of income support measures such as the reloadable Spend Local card.

Should another lockdown be required, the Co-Funded Payroll Scheme (CFPS) could provide more targeted and tiered support to those sectors disproportionately affected by social distancing requirements. Sentiment in future business activity for hotels, restaurants and bars was 54 percentage points below the three-year average in the September BTS, while the future employment indicator came in at -66 percentage points. Capacity utilisation remains weak in the non-finance sector as well. Given that the uptake of the CFPS to date has been lower than expected, the tapering of the subsidy could potentially be delayed for those sectors facing the greatest uncertainty or distress.

The government will need to remain agile and responsive to circumstances as they evolve in the months ahead. Enhancing productivity will be key if the standard of living for Jersey residents is to improve over time. The Fiscal Stimulus Fund and Economic Recovery funding should support human capital development through diverse pathways for education and workforce retraining, particularly in areas relating to innovation and sustainability. Finance professionals are not immune to the structural changes highlighted by the Plan either – “the increase in remote working provides a warning against complacency of many roles remaining in Jersey in the long term.” Since 1998, the financial services sector has reduced its share of economic output from more than half to just under 40% but its influence on the island remains significant.<sup>16</sup>

The lockdown and subsequent restrictions on activity have and will continue to impact people and businesses in different ways. Fiscal policy should create a level playing field for everyone, not least the start-ups and entrepreneurs who are often at the forefront of a post-crisis recovery. Unlike during the early phase of the pandemic when it was appropriate to cast a very wide net of policy support, subsequent interventions will need to become more nuanced if they are to remain affordable. Not all businesses and jobs can, or should, be saved either. Meanwhile, the government should closely re-examine alternatives to the

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<sup>15</sup>

<https://www.gov.je/SiteCollectionDocuments/Government%20and%20administration/R%20BTS%20Sep%202020%2020201022%20SJ.pdf>

<sup>16</sup> <https://opendata.gov.je/dataset/national-accounts>

proposed Infrastructure Fund given existing capacity constraints in the local construction sector that have challenged prior year spending plans.

Importantly, measures should be taken to monitor and combat fraud and tax avoidance. Such activity may become more common when customary checks and balances made during the initial claims process are not possible to expedite the issuance of payment.


## 6. Conclusion

The Government Plan 2021-24 charts an ambitious course for Jersey as it navigates its way through the uncharted seas of the Covid-19 pandemic, Brexit and beyond. Increasingly tight budget constraints due to the scale of the government's initial response coupled with a sharp decline in economic activity will challenge the island's finances for years to come. In contrast to many other jurisdictions, however, Jersey benefits from a substantial net asset position and fiscal buffers that have helped it maintain a high credit rating. Although this makes additional borrowing an attractive financing strategy, there is a risk that a sustained financial market correction could jeopardise Jersey's public finances in the long-term.

Given that pandemic-related risks have not yet subsided and that an approved vaccine is not yet available, there remains scope for the government to articulate clearer contingency plans on how it intends to address multiple crises. Embedding what was initially conceived as a stand-alone Recovery Plan into the issuance of another Government Plan may later be viewed as a missed opportunity for formalising what could have been a comprehensive emergency response strategy for the island. Each crisis may be different but the framework for a coordinated policy response can be quite similar. Future external shocks might include a cyber-attack, bioterrorism or a global trade war.

There is further scope for Jersey to diversify its economy away from financial services, especially given the reliance of its public finances on the performance of financial markets. Supporting the non-financial sector would help to attract and retain a younger and less transitory workforce which will be needed to fund public services for an ageing population. Without skilled tradespeople, Jersey will find it difficult to deliver on its capital spending agenda or even to build the houses that would make living on the island more affordable. Advancing the sustainability and climate change agendas in a way that aligns with Jersey's distinctive history, heritage and culture may benefit from a community perceived as fairer and less unequal as well.

To realise Jersey's potential, the government must continue to communicate actively with all its inhabitants. Businesses need to be consulted early and often especially during periods of crisis as they can be vital conduits for on-the-ground information. Citizen engagement too can be enhanced by recognising their needs early on and delivering on improved outcomes. To protect the island's future, Jersey must continue to cherish the diversity in its people and remain an inclusive community where they will want to work and live.



77 Mansell Street, London E1 8AN  
+44 (0)20 7543 5600

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