STATES OF JERSEY

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BUDGET 2008 (P.164/2007): THIRD AMENDMENT

Lodged au Greffe on 20th November 2007
by the Deputy of St. Ouen

STATES GREFFE

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In paragraph (b), for the word“£25,000,000” *insert the word* “£38,000,000”.

DEPUTY OF ST. OUEN

REPORT

Background

As part of the overall fiscal strategy the States agreed to establish a Stabilisation Fund and was included in a new fiscal framework for Jersey as required by the economic growth plan.

The objectives in setting up this new framework were to –

- Contain inflation.
- Maximise the economic potential of the Island.
- Create an effective macroeconomic policy framework that can improve economic stability in a small island in a currency union.
- Put in place a transparent and credible framework that is both pragmatic and clear to all.
- Make fiscal policy overall more countercyclical and manage the revenue streams from the financial services industry in a manner that enhances economic performance.
- Make provision for review of the framework as experience is gained in its operation in order that it can be strengthened and improved.

The States economic growth plan set out the importance that long-term economic stability has in creating the conditions for economic growth and low inflation which ultimately benefits all residents.

A critical part of that growth plan was to provide a new framework representing a clear break with the past. A key requirement for economic growth is the need to provide a stable economy for businesses and consumers to make decisions in, as a volatile economic cycle of boom and bust imposes costs on the economy which is likely to undermine efficiency and economic growth in the medium to longer term. While it may be tempting in the short term to allow the economy to grow rapidly, there are risks, especially if there is limited or no spare capacity in the economy. Any sustainable growth policy is required to focus on consistent growth ensuring that attention is paid to improving the supply side of the economy and not just the demand side.

Excessive growth leads to accelerated inflation, and the only way for the economy to adjust is generally through a recession. Inflation is therefore bad for economic growth and therefore certain mechanisms must be in place to ensure that low and stable inflation is maintained. This is especially important to the Island, as the local economy is dominated by the performance of the finance industry and the revenue it generates. What must be avoided is a situation where the finance industry is performing strongly and the higher taxation receipts delivered are simply fed back into demand in the economy, through higher government expenditure thereby creating inflationary pressure. This is equally applicable to spending windfall gains such as those identified recently.

Key components of the Island's fiscal policy are the new Stabilisation Fund and the balance between States' taxation revenue and expenditure. The general principle of a Stabilisation Fund is to accumulate revenues during periods of strong economic performance in order to compensate for poorer performance in future years. For the Stabilisation Fund to be effective it will need to have sufficient funds to be able to offer some real insulation against an economic downturn. The fund is not designed to prevent economic downturn but to allow funds to be used to either maintain valuable expenditure programmes or reduce taxes that might partly offset some of the negative consequences of a downturn. With the uncertainties over the impact of 0/10, the introduction of GST and the possible adverse effect of the "credit crunch" in the global financial sector on our local economy, it is clear that we should take the opportunity to build up this fund as quickly as possible.

In recent months, the latest financial forecasts have shown a marked improvement than those forecast 12 months ago. At that time, the financial forecast was showing a predicted deficit of £3,000,000 in 2007; however the most recent forecast now shows a surplus of £38,000,000 in 2007 and further improvements in 2008. It should be noted that the Minister for Treasury and Resources acknowledges that this major change in fortune is due, for the most part, to improvements in the economy as a result of economic growth exceeding expectations. With this in mind, the Minister proposes to transfer £25 million to the recently created Stabilisation Fund. The question States members must ask themselves is whether this is enough and why not the entire surplus of £38 million?

Estimated unspent balances in hand at 31st December 2007 held in the Consolidated Fund have increased from approximately £32 million shown in last year's budget to £78.5 million. This is forecast to rise to £111.6 million by 31st December 2008 as shown in Summary Table D on page 33 of the draft budget statement.

Whilst it is obviously important to ensure that sufficient funds are retained in the consolidated fund, it is my view that these sums are excessive and can be reduced by increasing monies transferred to the Stabilisation Fund. It should be pointed out that the forecast figure of £111.6 million already includes the transfer of £25 million proposed by the Minister for Treasury and Resources. This figure would reduce to £98.6 million if this amendment is accepted.

It is useful at this point to recognise the relationship between the Consolidated Fund and the Stabilisation Fund. The Consolidated Fund basically operates like a current account, used for the day-to-day funding of all government expenditure; whereas the Stabilisation Fund is classed as the savings account into which funds would be transferred in times of plenty, and out of which they could be transferred when specific needs arise. Target levels for these funds are usually set at between 15-20% of government spending, which would mean that in the case of Jersey the fund should be built up to a level of between £75-£100 million. Presently the fund currently stands at £32 million so, if members are minded to support this amendment, the result would be that this fund would increase to £70 million or close to the minimum required rather than the proposed £57 million.

Summary

With the significantly improved tax revenues expected in 2007 and 2008, this Assembly is able transfer the whole of the 2007 forecast surplus to the Stabilisation Fund. As stated earlier, the main purpose of the Stabilisation Fund is to provide greater protection to residents and businesses alike from the effects that any future economic downturn might bring. Members need to be aware that even with the increases in tax revenues and the extra income generated from the introduction of GST, forecasts are still showing deficits in the medium to longer term. By acting now and setting aside money in the Stabilisation Fund, the States should be able to allay some of the concerns over future increases in taxes and be able to maintain the GST rate at 3% over a much longer period. However, members must recognise that the Stabilisation Fund makes up only part of the fiscal strategy: if we are to achieve balanced budgets and a sustainable financial position, then public spending must be adhered to in order to achieve our target of low inflation. Importantly, this also means that current spending limits must be adhered to as all forecasts are based on this assumption.

Taking all the above into consideration, I would like to propose that the amount to be transferred into the Stabilisation Fund be increased from the proposed £25 million to £38 million, and I hope that members will support this amendment.

Financial/manpower implications

There are no financial or manpower implications for the States arising from this amendment.