Jersey's Fiscal Policy Panel

Senator Alan Maclean
Minister for Treasury and Resources
Cyril Le Marquand House
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1 March 2017

Dear Minister

Economic Assumptions

Please find attached the latest set of central economic assumptions (figure 1 attached) which the Panel has overseen for the purpose of updating the States financial forecasts. This is in keeping with our responsibilities under the Council of Ministers' Fiscal Framework.

In arriving at these assumptions we have considered the latest developments in the Jersey and international economies. At the time of our Annual Report in August 2016 we lowered our economic growth forecasts for Jersey for 2016 and 2017. In doing so we had tried to reflect the fact that despite some improvement in a number of economic indicators in 2015 there was considerable uncertainty regarding the likely short- and long-term economic implications of the UK's exit from the EU, and the impact on Jersey.

Since that report there have been continued positive developments in the Jersey economy. In particular:

- Real GVA growth in 2015 turned out to be higher than expected at 2.0%. This was a result of strong growth in the non-finance sector which grew by 5%, more than offsetting a fall of 1% in financial services.
- Total employment growth in the year to June 2016 was 2.1%, with employment reaching the highest level on record (60,320). This suggests that employment growth in 2016 will turn out to be significantly higher than the 0.5% we suggested last August.
- Headline inflation in Jersey ended 2016 lower than expected at 1.9% in December. Although there may have been temporary factors holding inflation down at the end of the year it still means that inflation averaged 1.7% in 2016 (compared with our previous assumption of 2.2%).
- The December 2016 Business Tendency Survey showed a general improvement when compared with the previous survey (March 2016). The headline business activity index recovered back to the level seen in the December 2015 survey and this reflected improvements in both the finance and non-finance sectors. However, the indicators for business optimism and future business and employment were generally below the level of the previous survey and those conducted in 2015. This was driven by trends in the non-finance sector, with the finance sector more optimistic and upbeat on future business prospects although not so on future employment.
- The Business Tendency Survey also contains information about financial institutions' expectations for profit growth in 2017 which suggests growth of 4.4% - higher than expectations in the 2016 survey and therefore higher than we previously anticipated.

The general picture presented by the latest economic data from Jersey is one where local economic conditions seem likely to be better than we previously expected in 2016 and 2017. We have therefore revised up real economic growth in these years to reflect the most recent trends.

The UK economy may also have performed better than expected in the period immediately following the UK referendum but we do not think this is reason to change the medium-term outlook for the Jersey economy. In particular, the medium-term challenges facing the Jersey economy have not changed and remain the same as at the time of our 2016 annual report:

- Uncertainty regarding the precise implications of the change in the UK's relationship with the EU for the Jersey economy;
- Continued economic, competitive and regulatory challenges facing the financial services industry in Jersey;
- The fiscal and economic consequences of the ageing population;
- The weakness in the rate of underlying productivity growth.

The Panel has not updated its analysis of the long-term trend rate of growth and degree of spare capacity in the Jersey economy, as there is no new information that would significantly impact our existing estimates. With slightly higher growth in 2016 and 2017 than previously forecast the amount of spare capacity in the economy may well be shrinking faster than we previously anticipated, although there is always considerable uncertainty around such analysis. At this stage any improvement in States finances that results from the higher economic growth should not yet be treated as if it were structural.

The overall policy advice from our annual report still holds. It remains important that the States continues to support the economy in the short term, particularly in such an uncertain environment. However, it is also just as important that rapid progress is made in achieving a more sustainable position in the medium term. This is irrespective of the exact future relationship between the UK and the EU.

If the UK's withdrawal from the EU has any structural implications for the Jersey economy and public finances then these will need to be addressed in the next MTFP period. However, as we said in our last annual report this view is contingent on the package of measures (or others of equivalent value) and capital expenditure set out in the MTFP Addition being delivered as planned.

It is therefore imperative that following the decision not to bring forward a new health charge that equivalent measures (expenditure and/or revenue) are put in place to deliver the same degree of fiscal tightening as previously planned.

I hope you find the economic assumptions and related comments helpful as you continue to develop your fiscal plans and consider your approach for Budget 2018.

Yours sincerely

Kate Barker (Chair)

Tera Allas and Francis Breedon

Figure 1: Economic assumptions
% change unless otherwise stated

	2014	2015	2016	2017	2018	Return to trend 2019	2020
Real GVA	4.9	***2.2***	1.5	1.0	0.0	0.0	0.0
RPI	1.6	0.6	***1.7***	2.7	3.0	3.3	3.3
RPIY	1.6	0.6	***1.7***	2.7	3.0	3.0	3.0
Nominal GVA	6.6	***2.9***	3.2	3.7	3.0	3.0	3.0
Company profits	12.3	***-0.7***	2.8	3.7	3.0	3.0	3.0
Financial services profits	19.4	***-7.6***	2.6	4.4	3.0	3.0	3.0
Compensation of employees	2.1	***5.9***	3.6	3.7	3.0	3.0	3.0
Employment	2.3	1.9	1.5	0.8	0.0	0.0	0.0
Average earnings	2.6	1.8	2.1	2.9	3.0	3.0	3.0
Interest rates (%)	0.5	0.5	***0.4***	0.3	0.4	0.6	0.8
House prices	3.0	4.0	***4.0***	3.0	3.0	3.0	3.0

New outturns in bold

August assumptions

	2014	2015	2016	2017	2018	Return to trend 2019	2020
Real GVA	4.9	0.9	0.4	0.0	0.0	0.0	0.0
RPI	1.6	0.6	2.2	3.3	3.0	3.3	3.3
RPIY	1.6	0.6	2.3	3.4	3.0	3.0	3.0
Nominal GVA	6.6	1.5	2.7	3.4	3.0	3.0	3.0
Company profits	12.3	-2.7	2.8	2.9	3.0	3.0	3.0
Financial services profits	19.4	-7.5	2.6	2.8	3.0	3.0	3.0
Compensation of employees	2.1	5.3	2.6	3.8	3.0	3.0	3.0
Employment	2.3	1.9	0.5	0.0	0.0	0.0	0.0
Average Earnings	2.6	1.8	2.1	3.8	3.0	3.0	3.0
Interest rates (%)	0.5	0.5	0.4	0.1	0.1	0.2	0.4
House prices	3.0	4.0	4.0	3.0	3.0	3.0	3.0

Change

	2014	2015	2016	2017	2018	Return to trend 2019	2020
Real GVA	0.0	1.3	1.1	1.0	0.0	0.0	0.0
RPI	0.0	0.0	-0.5	-0.6	0.0	0.0	0.0
RPIY	0.0	0.0	-0.6	-0.7	0.0	0.0	0.0
Nominal GVA	0.0	1.4	0.5	0.3	0.0	0.0	0.0
Company profits	0.0	2.0	0.0	0.8	0.0	0.0	0.0
Financial services profits	0.0	-0.1	0.0	1.6	0.0	0.0	0.0
Compensation of employees	0.0	0.6	1.0	-0.1	0.0	0.0	0.0
Employment	0.0	0.0	1.0	0.8	0.0	0.0	0.0
Average Earnings	0.0	0.0	0.0	-0.9	0.0	0.0	0.0
Interest rates (%)	0.0	0.0	0.0	0.2	0.3	0.4	0.4
House prices	0.0	0.0	0.0	0.0	0.0	0.0	0.0

OUTTURNS