FISCAL POLICY PANEL

2025 REPORT

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The Fiscal Policy Panel ('the Panel') consists of three members:

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- Prof. Francis Breedon
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1. Executive Summary

- The States of Guernsey ('the States') is currently reviewing its Fiscal Policy Framework and has specifically sought advice from the Panel on the management of capital expenditure and investments within its fiscal rules.

- The Panel defines permanent fiscal balance as ensuring that revenue, spending, infrastructure investment and reserves are maintained over time without resorting to emergency measures or the accumulation of unsustainable debt.

- Guernsey is a small open economy with a low tax to GDP ('Gross Domestic Product') ratio. It also spends less as a percentage of GDP on public service provision and infrastructure investment even when compared with other low tax economies.

- Infrastructure spending supports economic productivity and growth which, in turn, supports fiscal sustainability. The power, water, telecommunications, transport and wider social infrastructure (such as schools, hospitals and housing) built now will underpin the future economic activity that contributes to stable revenues and sustainable public finances.

- Chronic underinvestment in Guernsey's public infrastructure is an increasingly binding constraint on growth, fiscal sustainability and living standards. The Panel's preferred target for infrastructure investment would be to average 3% of GDP over the medium- to long-term. This is higher than the current 2% target, which itself has not been consistently met.

- Much of Guernsey's critical infrastructure formally 'sits' on the balance sheets of quasi arm's-length companies. Effective oversight and regulation are required to ensure that these infrastructure assets are maintained over time to avoid public bailouts in the face of crises. Where investments by these entities constitute core infrastructure for the Island, the public contribution towards capital spend by these entities could count towards meeting the 3% target.

- Delays and slippage in the progression of major capital programmes is common, but this has been particularly evident in Guernsey. The Panel recommends that the States seeks to enhance its existing prioritisation process for major projects and implement a longer-term planning horizon to support a more stable flow of projects through the portfolio, and minimise 'stop/start' disruptions.

- Revenues in recent years have been insufficient to support the Panel's definition of permanent fiscal balance. As highlighted in the Panel's previous report and in its comments on the Major Projects Portfolio Review Policy Letter, the current tax base, as it exists in 2025, cannot sustainably support both the current profile of service provision and the level of infrastructure investment needed to maintain the capital stock.

- Tax reforms currently proposed (but not yet implemented) are an important step towards long-term fiscal sustainability, including the ability to fund Routine Capital and Major Projects Portfolios (at an investment level of 2% of GDP), *if they are implemented*. However, the Panel's preferred target is 3% of GDP.

- Without implementation of the agreed tax reforms, progressing even the minimum level of infrastructure investment needed is projected to result in the complete depletion of the States' unallocated financial reserves, resulting in a deteriorating net debt position without the revenues available to stabilise the situation.

- Although Guernsey has a relatively lean public sector, an ageing population means there are foreseeable increases in expected costs around health and social care. Recent proposals to increase contributions to the fund supporting States' pensions – if they are implemented – would go a long way towards closing the gap, but may not be sufficient.

- The Core Investment Reserve is also significantly below (less than one third of) its target. Research suggests a buffer of 30% - 60% of GDP would be needed for this reserve to properly serve as protection against a severe economic shock.

2. Introduction

This report examines two key issues facing Guernsey: infrastructure investment and fiscal sustainability. These topics are often framed as separate concerns but are related.

Future fiscal sustainability depends on a robust, growing economy, which in turn requires infrastructure investment today. The power, water, telecommunications, transport and wider social infrastructure (such as schools, hospitals and housing) built now will underpin the future economic activity that contributes to stable revenues and sustainable public finances. Similarly, today's fiscal position is shaped by past infrastructure decisions — previous investment decisions are one driver of current economic productivity, government revenues and the fiscal space available for new spending.

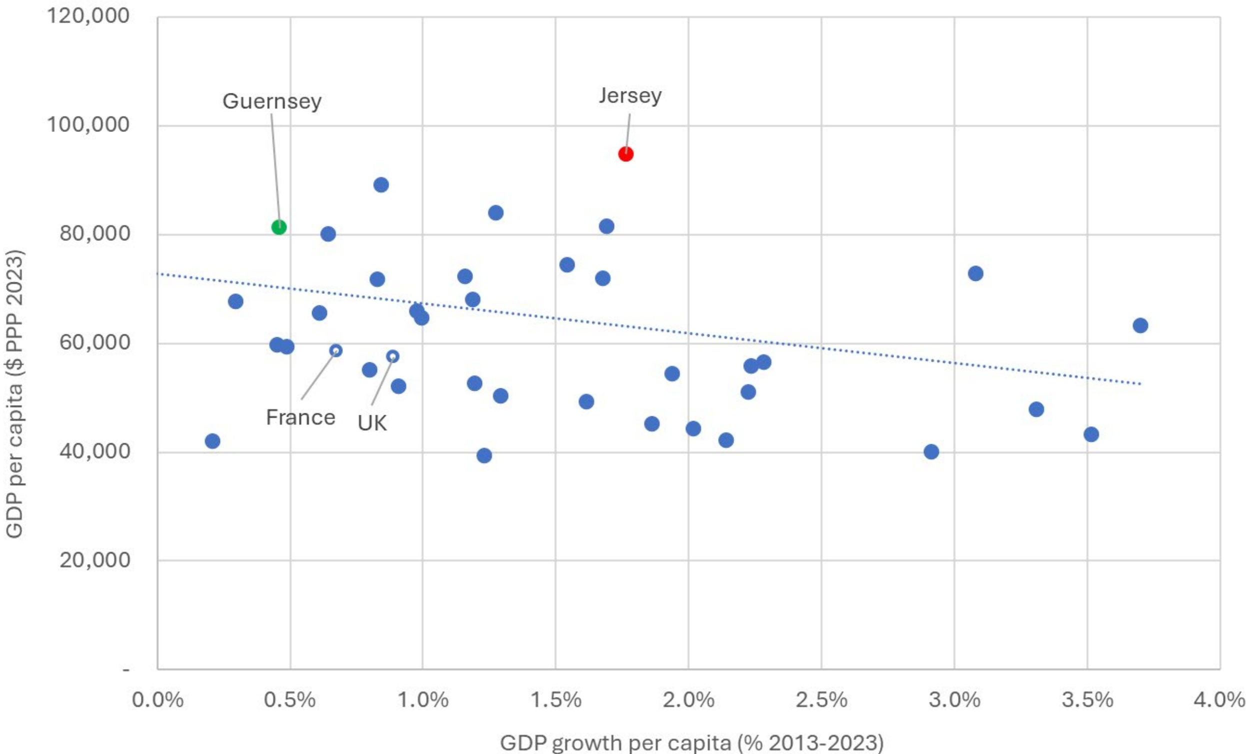
Well-designed financing models including phased funding, debt financing, user (or other) fees and the mix of public and private funding can help spread infrastructure costs over time, including to align with the arrival of benefits. However, tax revenues remain central to fiscal sustainability and infrastructure investment, both today and in the future.

In Guernsey's unique economic context, fiscal sustainability must take a long-term perspective. As a small island economy, Guernsey is less diversified and could be more affected by unexpected changes in local or global conditions. It is also facing some known pressures. An ageing population will place increasing demands on healthcare, pensions and social services, making it essential to ensure that savings, reserves and other public assets are sufficient to meet future liabilities. A weak and deteriorating fiscal position has led to a significant shortfall in public investment which in turn has weakened revenue growth and exacerbated the fiscal problems Guernsey faces. Action is now required to break this vicious circle.

3. Guernsey's Economic and Fiscal Structure

Guernsey is a small, rich economy characterized by slow growth. Real annual GDP growth per capita averaged 0.4% a year between 2013 and 2023. This is typical of wealthy economies (see Fig.1) but presents significant challenges for fiscal policy. Whereas higher growth can erode the value of debt relative to GDP, in a low growth environment the reverse is true: government debt becomes more onerous over time. The result is that fiscal sustainability in slow-growing economies typically requires governments to run fiscal surpluses.

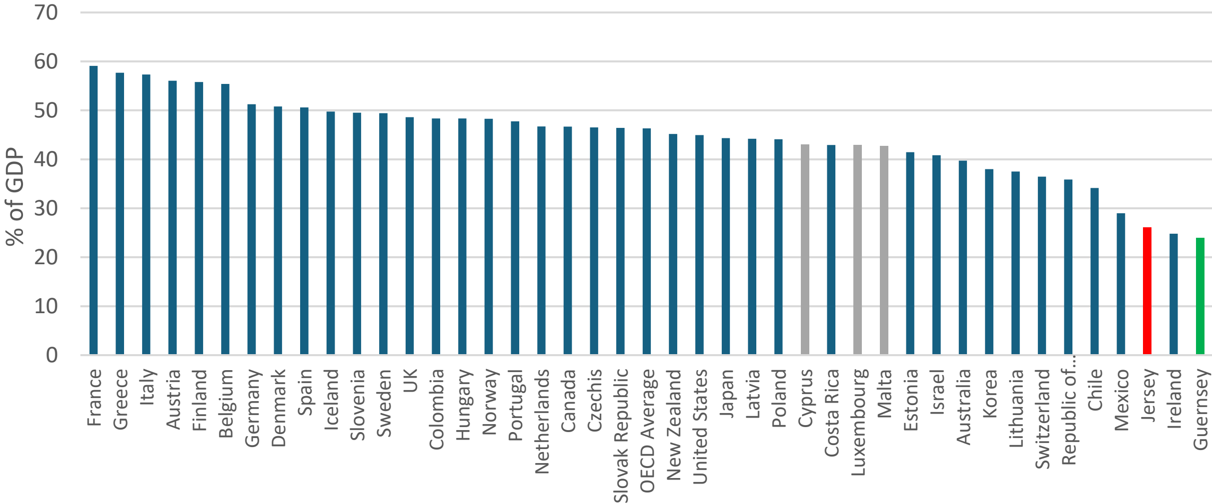
Fig.1 - Average annual per capita GDP growth vs GDP (2013 – 2023)[1]



OECD data demonstrates that, at just 23% of GDP, government spending in Guernsey is low relative to other wealthy nations, including other small island states (Fig.2).

[1] https://www.imf.org/en/Publications/WEO/weo-database/2024/April/

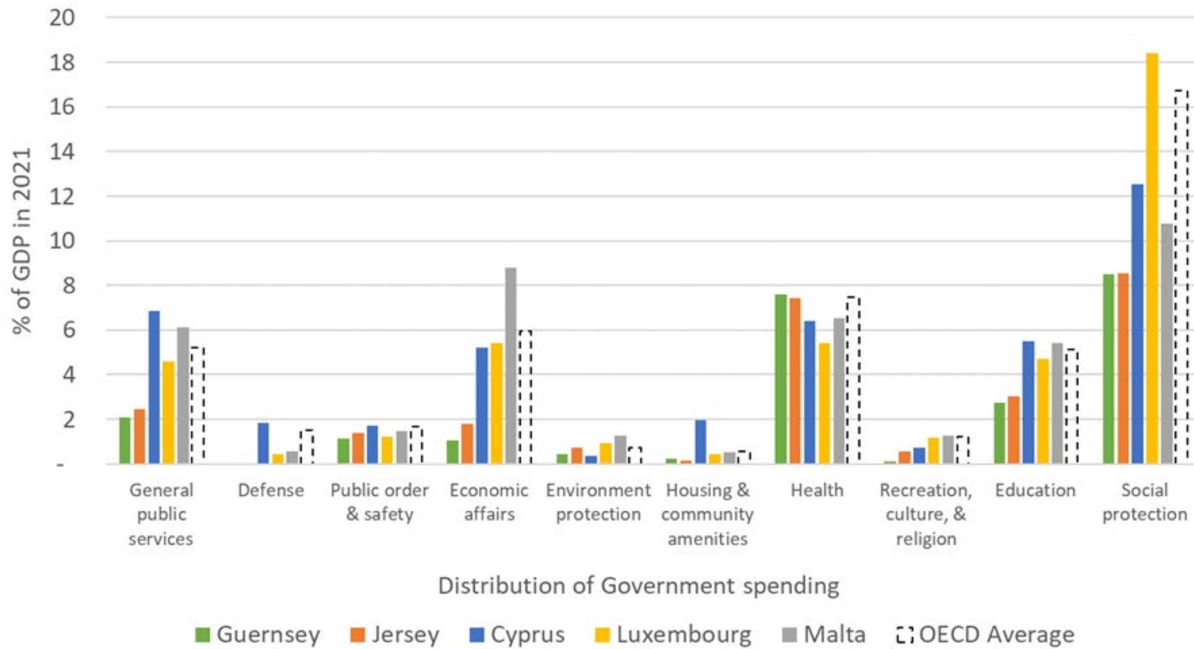
Fig.2 - OECD Government Spending as a % of GDP, 2021[2]



Guernsey spends less as a percentage of GDP on most types of services when compared to other economies. In particular the low level of spending on social protection is one key reason why Guernsey's overall spend is well below the OECD average. However, spending on education and other government services is also well below OECD averages and most of the comparator jurisdictions included in Fig.3. Only on health services does Guernsey's spending match the OECD average.

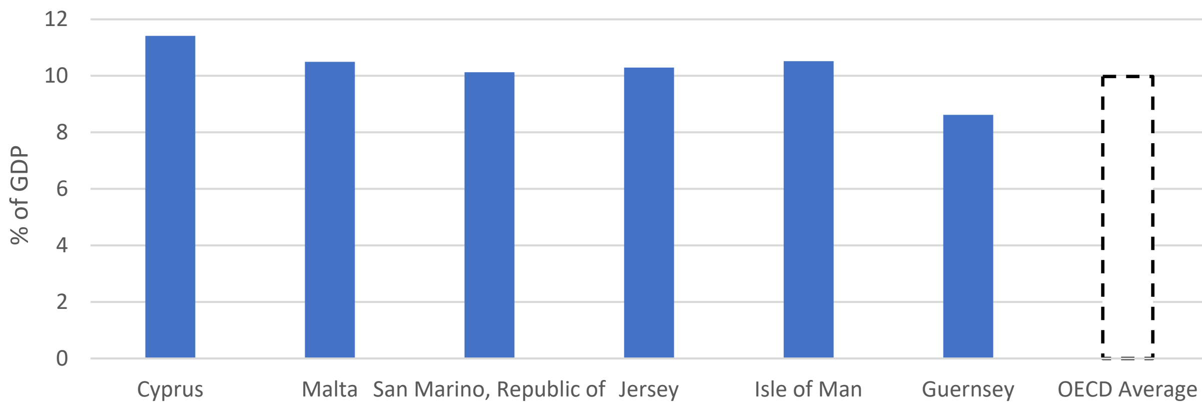
[2] OECD National Accounts Statistics (database), IMF Government Financial Statistics - COFOG expenditure as a % of GDP, Statistics Jersey and States of Jersey Accounts, States of Guernsey

Fig.3 - Government spending by category as a % of GDP, 2021[3]



Given the labour-intensive nature of most public services, it follows that Guernsey's public sector wage bill is also significantly lower as a percentage of GDP than other small jurisdictions and the OECD average (Fig.4).

Fig.4 - Public sector wage bill comparison as a % of GDP, 2022[4]



At 32%, Guernsey's older adult dependency ratio is already higher than the OECD average, meaning that the population has a higher balance of older people to those of working age than

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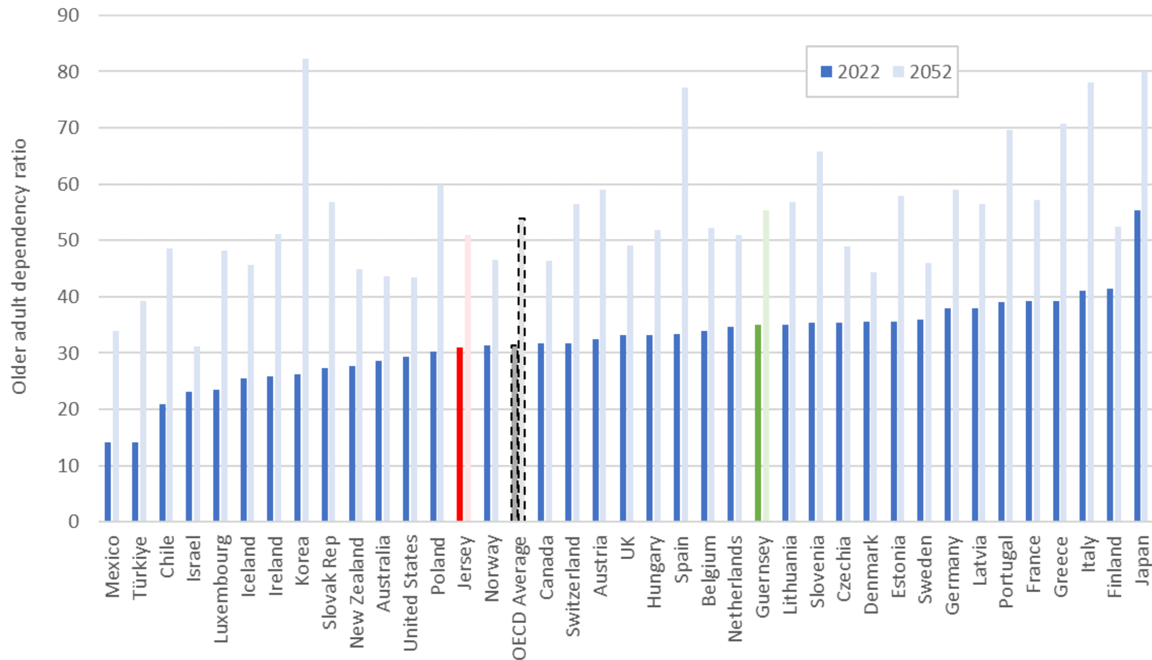
[3] IMF Government Financial Statistics - COFOG expenditure as a % of GDP, Statistics Jersey and States of Jersey Accounts, States of Guernsey.

[4] IMF Government Financial Statistics - Compensation for employees, States of Jersey Accounts, Isle of Man Central Management Accounts – March 2023, States of Guernsey, OECD National Accounts at a Glance.

most jurisdictions (Fig.5). This partially explains the relatively higher expenditure on health services in Guernsey.

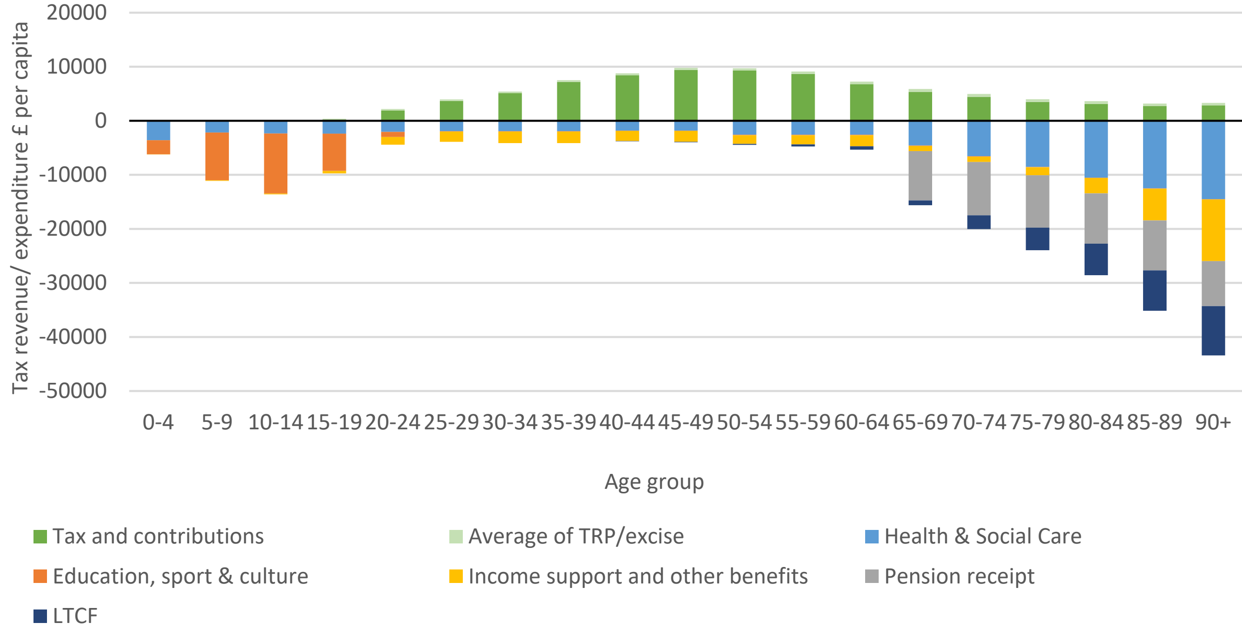
Fig.5 - Dependency ratio in Guernsey vs other jurisdictions (2022 & 2052)[5]



Like almost all higher income nations, Guernsey's older adult dependency ratio is expected to continue to rise well into the middle of this century, creating an increasing pressure on health and other services. The higher per capita spend in providing necessary services to older people (Fig.6) places upward pressure on government spending. That is already observable in the cost of the States' pension provision and is becoming increasingly evident in health and care services.

[5] Demography - Old-age dependency ratio - OECD Data - Note that the definitions used by the OECD differ from those typically used in Guernsey and Jersey, and as such Guernsey and Jersey's dependency ratios have been recalculated to be consistent with these.

Fig.6 - Tax revenue/(expenditure) per capita by age group[6]



4. Permanent Fiscal Balance

The Panel's brief for 2025 is set in the context of a review of the States' primary strategic fiscal policy – the Fiscal Policy Framework ('the Framework'). Specifically, the Panel is asked to consider the role of infrastructure investment and the States' financial assets in achieving 'permanent fiscal balance'. The initial step is to define and set out criteria for maintaining a permanent fiscal balance in Guernsey.

The Panel's view is that maintaining permanent fiscal balance entails consistently aligning spending, revenue, infrastructure investment and reserves over time[7] so that:

- The budget remains sustainably/smoothly balanced without resorting to lumpy adjustments, emergency measures or the accumulation of unsustainable debt;
- Reserves and cash holdings are maintained at a sufficient level to cover expected liabilities and to provide resilience against major shocks; and
- Investment in the capital stock (infrastructure) is maintained at a consistent level over time relative to the size of the economy.

Thus, maintaining permanent fiscal balance is simultaneously:

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[6] Data from States of Guernsey's Strategic Finance Team.

[7] The term 'over time' is deliberately flexible. Spending, revenue, investment and reserves will fluctuate and need to be balanced over the medium to long-term, but not necessarily on a day-to-day or even year-to-year basis.

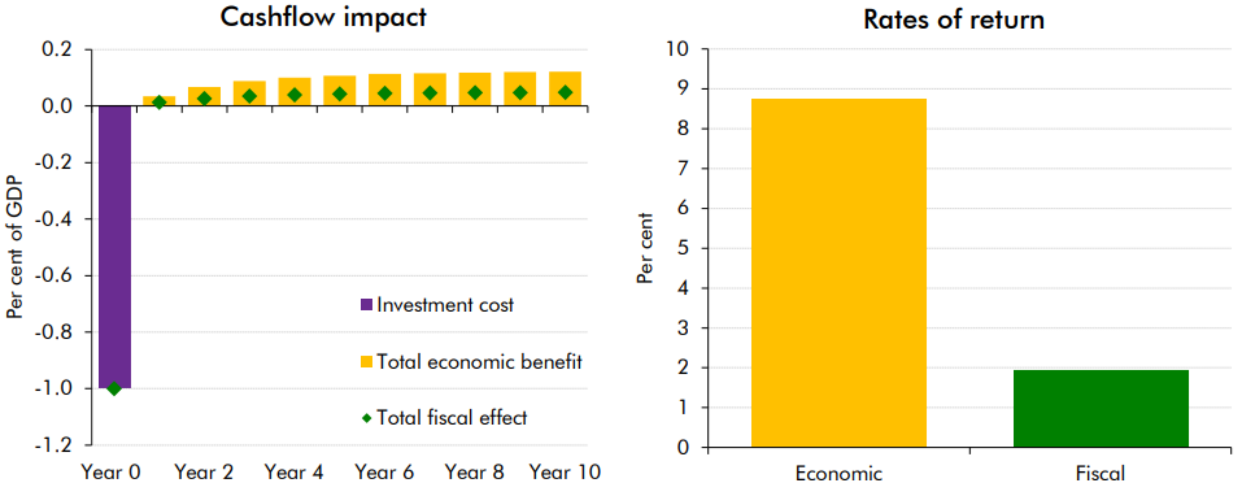
- an annual budget issue, ensuring money received is consistent with the plans for money spent;
- a balance sheet maintenance issue, ensuring that the States' stock of assets, both financial and physical, and its liabilities are managed sustainably; and
- a governance and regulatory issue, as many critical infrastructure assets formally sit on the balance sheets of private companies (e.g. in telecoms) or arm's-length entities (e.g. ports, electricity).

This definition supports an infrastructure investment strategy which would seek to progress all projects that meet a defined threshold of economic or social return and that these should be prioritised within budget constraints and (construction and planning) capacity to deliver. Notwithstanding those budget constraints, public sector infrastructure spending should account for about 3% of GDP for it to continue to play its role in supporting the cycle described above: infrastructure spending supports economic productivity and growth which, in turn, supports fiscal sustainability.

Government plans should be assessed against this investment rule over time. As discussed below, predictability and stability are important features of maximising the value of infrastructure and return on investment. Permanent fiscal balance (as described above) should be met by consistent effort and planning across many years. Consistency is preferable to significantly over-shooting in one year and under-shooting in another.

It is important to distinguish between direct fiscal (or financial) and broader economic returns to infrastructure investment. Some projects may offer a significant economic benefit but very limited direct financial return to the public purse. For instance, the benefits from upgrading Guernsey's school estates accrue to individuals and families who enjoy better facilities and improved skills but may not deliver immediate financial returns to the public sector. Other projects offer limited fiscal or economic return but may still be necessary – for example to comply with international standards for handling waste. All (beneficial) projects, whether they generate financial return or not, should contribute to future productivity, growth and standards of living which may ultimately flow through, in part, to the public sector in the form of increased financial returns.

Fig.7 - UK Office for Budget Responsibility ('OBR') analysis of rates of return on public investment[8]



Evaluating large scale projects is challenging, but the economic consensus is that investment has long-term economic benefits. The OBR assessment of the value of public investment is that it generates significant returns – with an average of 2.4% added to GDP for every 1% GDP of investment over a period of ten years. By this assessment, Guernsey's under-investment in infrastructure represents a significant loss of potential economic growth.

5. Defining public infrastructure investment in Guernsey

Making a clear recommendation about the minimum level of public capital investment as a share of GDP first requires a clear demarcation of what is 'included' and what is 'excluded' from the definition of infrastructure. This is especially important in Guernsey due to the balance of 'core' government infrastructure alongside a series of incorporated and unincorporated entities – a mix often seen in small economies where government involvement is often required in areas running below minimum efficient scale. Economic growth depends on the total physical capital stock available to the economy, regardless of whose balance sheet some assets sit on. However, permanent fiscal balance for the States may focus more narrowly on the public sector balance sheet, while assessing the risk that assets which are not formally on the public sector balance sheet may end up there in times of crisis.

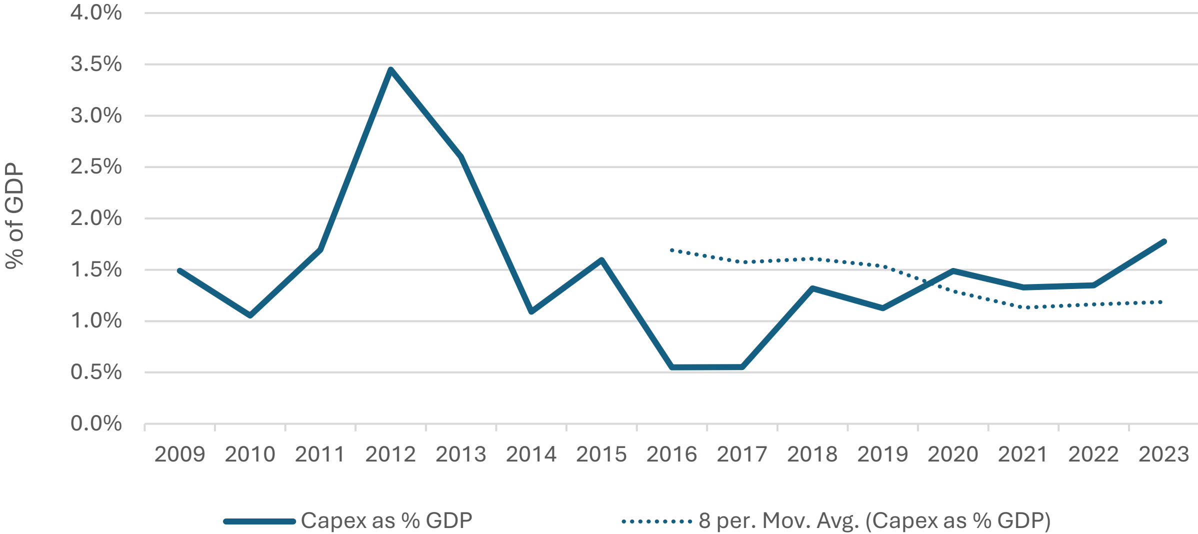
The States currently defines infrastructure investments under two categories:

- Routine Capital, which covers projects with a value of less than £3m. Typically this will include the replacement of vehicles, and medical and IT equipment.
- Major Projects, which covers projects with a value of more than £3m. This will incorporate significant building developments, major IT investments and transformation.

[8] https://obr.uk/docs/dlm_uploads/Public-investment-and-potential-output_August-2024.pdf

These investments are captured within 'core' government services. The formal requirement under the principles of the Framework is that the States spends on average 1.5% of GDP over a rolling four-year period and 2% over a rolling eight-year period. The actual capital spend on these streams has averaged 1.5% since 2009 and 1.2% over the last eight years. Only in 2012 and 2013, when two large scale projects (the construction of a school and the rehabilitation of the airport runway) were being completed simultaneously, has the States achieved 2% of GDP spend with its direct investments.

Fig.8 - Capital expenditure by the States of Guernsey as % GDP, 2009 - 2023



The current definition of infrastructure investment (reflected in Fig.8) does not include the capital spend made by a wider range of (incorporated and unincorporated) entities captured under the States of Guernsey Group Accounts (unless these are supported directly from the States' own reserves). From the publication of the 2024 accounts, the entities that will be included within the statistics for public sector capital spending are:

- Unincorporated entities:
  - Guernsey Dairy
  - Guernsey Ports
  - Guernsey Water
  - Guernsey Waste
  - States Works
- Incorporated entities
  - Cabernet Limited/Aurigny Air Services
  - Guernsey Electricity
  - The Guernsey Housing Association ('GHA')
  - Guernsey Post

These entities are included within the group accounting boundary on the basis that the States of Guernsey is considered to have decision making control over them. In some cases, these entities make significant investment in the Bailiwick's core infrastructure.

Fig.9 - Capital expenditure by entities associated with the States of Guernsey, 2018 - 2023

	Capital Expenditure (£m)					
	2023	**2022**	**2021**	**2020**	**2019**	**2018**
Guernsey Dairy	0.4	0.2	0.1	0.6	1.1	0.3
Guernsey Ports	2.9	5.1	5.2	1.0	2.0	1.1
Guernsey Water	5.9	5.6	4.0	4.4	4.1	5.0
Guernsey Waste[9]	0.2	0.0	0.0	0.0	0.0	-
States Works	0.9	0.6	0.9	2.3	1.2	1.6
Cabernet Limited/Aurigny Air Services[10]	1.4	1.0	0.4	-	-	-
Guernsey Electricity[11]	12.9	4.6	6.4	22.1	16.9	10.4
Guernsey Housing Association	5.2	10.4	9.0	10.6	15.7	14.9
Guernsey Post[12]	3.4	2.5	1.0	1.1	0.8	0.6
Total investment by group entities	**33.2**	**30.0**	**26.6**	**42.1**	**41.8**	**33.9**
As % GDP	**1.0%**	**0.9%**	**0.9%**	**1.5%**	**1.4%**	**1.2%**

International comparisons are complicated by the fact that slightly different entities are included within definitions of public spending in different countries. For example, in many jurisdictions where electricity and housing are fully outside the public sector, those investments will not be captured in records of public sector spending. This is discussed further below.

A significant portion of the investment made by these entities comprises core national infrastructure of the Bailiwick. However, some of this investment is driven by the purely commercial activities of these entities and could not be viewed as public infrastructure[13]. Recent examples of critical infrastructure developed by the trading entities includes:

- **Guernsey Electricity:** The installation of a new undersea cable connecting Guernsey to the European electricity grid, which secures the majority of Guernsey's electricity requirements (2019);

[9] Established on 1 January 2019.
[10] Information not available prior to 2021.
[11] 2018 and 2019 figures adjusted to reflect change in year end from 31 March to 30 September with effect from 2020.
[12] Financial year ends 31 March.
[13] One example is the recent development of warehousing and transport services by Guernsey Post which will facilitate deliveries from companies that would not typically deliver to Guernsey.

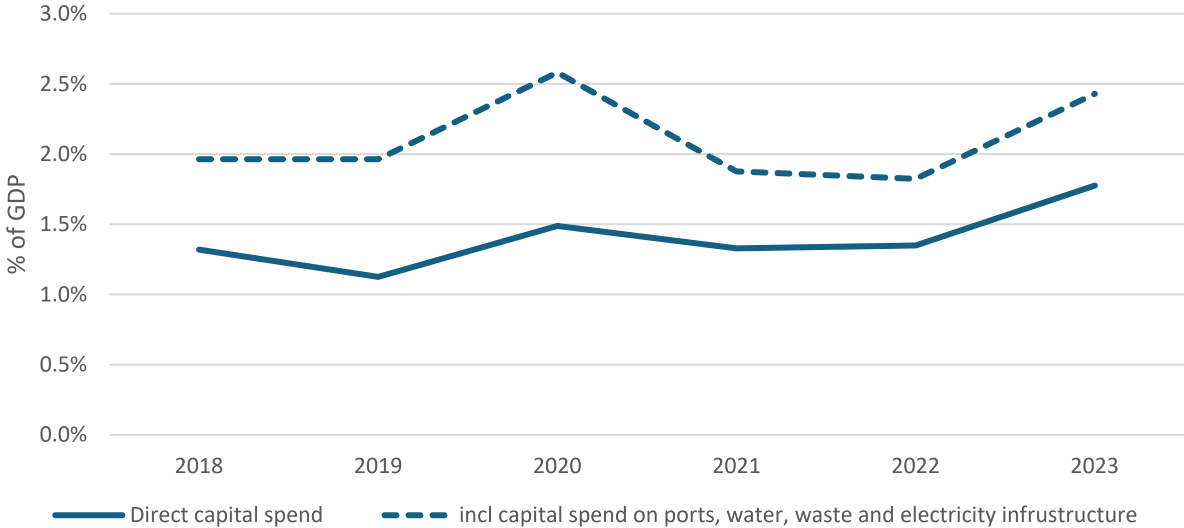
- **Guernsey Water:** The installation and upgrade of wastewater management systems including replacing the long sea outfall (2015);
- **Guernsey Waste:** The creation of a waste transfer plant to allow the sorting and export of solid waste (2019);
- **Guernsey Housing Association:** All social rental and partial ownership development (with some grant funding issued from the States of Guernsey).

The result is that some – but not all – of the investment made by these entities should be included within the consideration for an appropriate level of investment for Guernsey.

The Panel's recommendation is that public sector investment should constitute about 3% of GDP consistently over time. This includes a range of investment in core strategic infrastructure that would not be captured within the 'public sector' in many other jurisdictions.

A precise disaggregation of 'public' versus 'purely commercial' investment undertaken by these trading entities lies outside the scope of this report. However, to give an indication of how this might impact the reported level of investment, Fig.10 incorporates the capital spend undertaken by Guernsey Ports, Water, Waste and Electricity, adding an average of 0.7% of GDP to the total spend over the past six years. This should be viewed as an upper bound of what might be incorporated; the value in reality should lie somewhere between.

Fig. 10. Capital expenditure by the States of Guernsey including Ports and utilities as % GDP, 2017 – 2023



Investment in housing would typically not be incorporated within public infrastructure investment. This is because the degree to which housing is subsidised varies significantly between jurisdictions, and most countries' affordable housing tends to be delivered by subsiding rents rather than direct capital investment. Housing should not compete for the same pool of capital funds because it can pay for itself either privately or with public support through the revenue

budget. The recommended level of investment, which is drawn largely from international comparisons, has therefore been established assuming investment in housing is outside of its scope.

Given the importance of housing infrastructure to Guernsey's economy and the challenges identified in Guernsey's housing market (see Box 1 on page 24), a significant amount of investment in housing is likely to be required in Guernsey. This is identified in the States' own policy priorities, and the States has set separate objectives for delivering housing. If the States wanted to include investment in social housing within the recommended level for investment in public infrastructure, the Panel's view is that this would be additional to the 3% recommendation because financing of new housing should be possible without it competing for capital funds.

6. Guernsey's infrastructure spending and its governance

The States aims to set the portfolio of the major projects it wishes to pursue near the beginning of each political term, with the intention that the portfolio will be carried through the political cycle without significant changes until the next election.

At the beginning of each States' term there are three categories of projects:

- **'In flight'** projects that are ongoing and committed from the previous term;
- **Priority** projects for the current term as identified by alignment with strategic priorities set out by the States and delivery of positive net benefits, based on a long list from all Committees and seeking to balance the size and timing of projects (to support deliverability and manage capacity); and
- **Pipeline** projects that need initial sign-off this term to allow preliminary steps (e.g. business case, to signal planning needs etc.) but would come back for a decision on prioritisation in a subsequent States' term.

Each major project has a sponsoring Committee which works with the Policy & Resources Committee ('P&RC') to agree a detailed business case, including funding requirements with Treasury officers. The States uses a standard five-case model (strategic, economic, financial, commercial, management cases) for projects of significant size.

The States is then asked to agree a total funding envelope for a recommended list of priority projects. The States provides P&RC the delegated authority to fund the progression of these prioritised projects up to the point of final investment decision (and to completion for anything under £5m).

This process is designed so that major projects are planned and implemented over a medium-term horizon with objectives determined at the outset of the political term. Delegated authority for P&RC to progress the agreed portfolio allows the programme to continue uninterrupted between periodical reviews. This should facilitate a continuous flow of projects through the

portfolio and predictability for the supply-chain involved in delivery. However, the recent reality has been that fiscal considerations have resulted in multiple changes in the funding envelope and a much more frequent review of the portfolio than is consistent with smooth progression of investment.

This process was revised in 2023 requiring P&RC to return to the States to seek dedicated approval to progress any project with a total spend of over £5m, resulting in the States debating the merits of individual projects. Fiscal constraints have also resulted in the review of the Major Projects Portfolio in 2023, when the extent of the programme was significantly curtailed, and again in 2025, with the Policy Letter[14] debated in February 2025 outlining plans to deliver the revised portfolio over a longer time horizon.

The Panel commented on the most recent Policy Letter that 'stopping and starting' large scale infrastructure projects is inefficient and costly. Frequent and unpredictable changes to the public investment pipeline - as experienced in recent years - harms delivery and often raises costs. The UK's National Infrastructure Commission ('NIC') identified frequent 'late-stage' revisions to projects and 'a failure to build [projects] fast' as key drivers of cost overruns[15].

The next planned debate of the overall envelope for funding is in 2026, after the next General Election. Tax reforms currently proposed (but not yet implemented) are an important step towards long-term fiscal sustainability, including the ability to fund Routine Capital and Major Projects Portfolios, *if they are implemented*.

Each edition of the Framework has included an indication of how much the States should be investing in infrastructure. The current edition states:

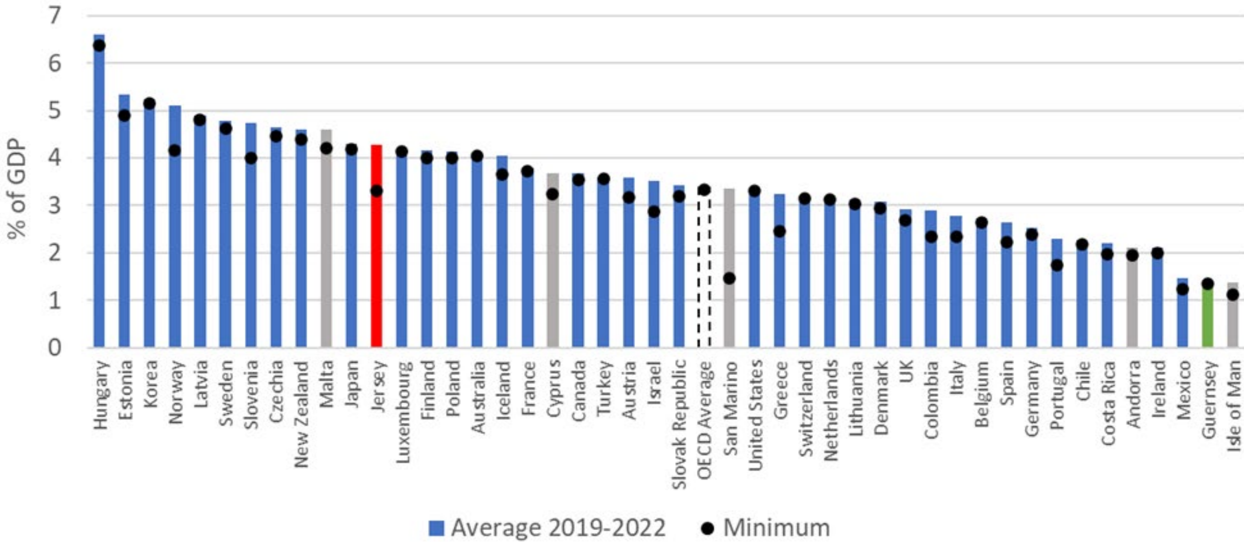
"Total capital expenditure over any States' term should be maintained at a level which reflects the need for long- and medium-term investment in infrastructure, and direct capital expenditure by the States should average no less than 1.5% of GDP per year averaged over a 4-year period and 2% per year averaged over any 8-year period."

This has generally been interpreted as referring to only the direct capital spend made from the States' own resources and does not incorporate investment supported by the States' trading entities.

[14] Major Projects Portfolio Review, dated 17 January 2025

[15] National Infrastructure Commission (2024). Cost drivers of major infrastructure projects in the UK. https://nic.org.uk/app/uploads/NIC-Costs-Report-Final-Oct-2024.pdf.

Fig.11 - Government investment in infrastructure as a % of GDP[16]

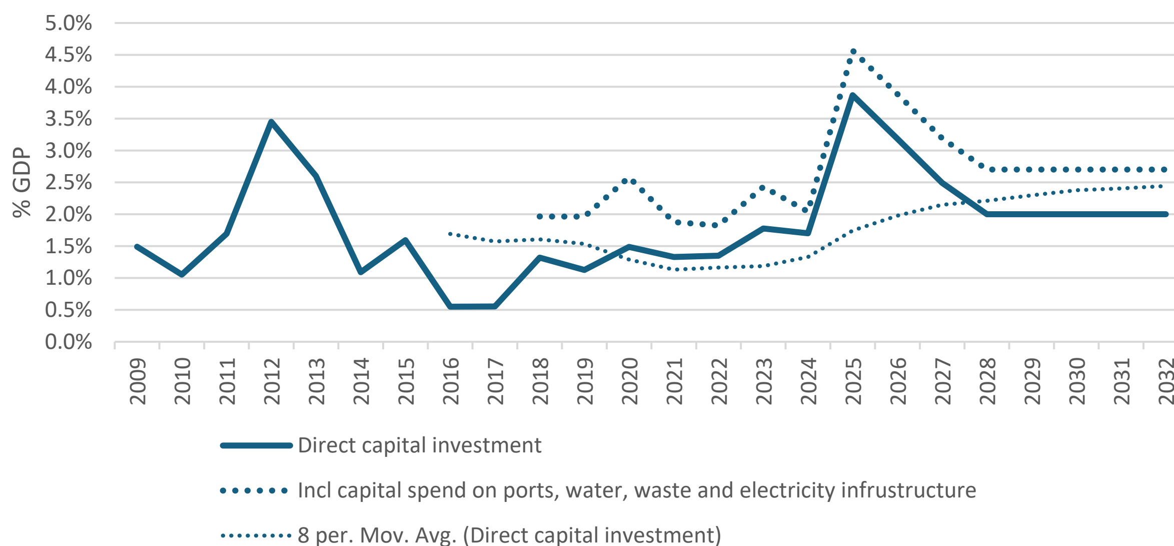


Guernsey's capital investment has fallen short of its own targets, averaging 1.2% of GDP from 2016 - 2023. It is also well below the OECD average and comparator economies, with a five-year average of 1.4%. Even adding the average of 0.7% of investment made by Guernsey's ports and the States' owned utilities in the past five years, Guernsey's level of investment would remain substantially lower than average.

This level of spending is insufficient to sustain the Island's capital stock and has contributed to a significant backlog of major projects that has accumulated over 15 years of underinvestment. If the States completes its current portfolio of 'essential' major projects as planned, direct capital spending could exceed 3% of GDP in 2025 and 2026, raising the eight-year rolling average above 2% by 2027.

[16] OECD National Accounts Statistics (database)

Fig.12. Government investment in infrastructure as a % of GDP[17]



While the modelling assumption is that, beyond 2027, spending will be maintained at an average of 2% of GDP (aligned with the current Framework principle), it is currently estimated that the total value of all projects that could be put forward by Committees for prioritisation is approximately £1bn. Many of these will not meet the threshold for prioritisation, but if half were to meet the required cost/benefit threshold for progression over a four-year period, the States would need to spend an average of £125m a year – more than one and a half times its current target and well over twice as much as its recent spend – to catch up.

A good infrastructure planning process

Infrastructure investment takes place over long periods of time: the infrastructure itself often takes years to build and the benefits are realised over even longer periods. As a consequence, good planning is crucial: stop-start decisions can increase direct costs (e.g. of materials and people) and indirect costs (from lower economic growth driven by bottlenecks that build up). Stop-start processes also create uncertainty which often leads to further delays as construction, engineering and other companies prioritise other projects.

Best practice emphasises properly planning the pipeline of projects in the first instance. In the UK, the NIC (working with the Infrastructure and Projects Authority) articulates the 'infrastructure gap' (through its National Infrastructure Assessment) and provides costed recommendations for closing the gap. Those costed recommendations have to sit within an overall budget defined by Treasury.

[17] OECD National Accounts Statistics (database)

A smaller economy like Guernsey may not need to involve so many institutions, but the result should be a transparent, public articulation of the pipeline of projects that fit within an agreed budget. While some elements of best practice are in place, the experience in recent years suggests there is a need for greater clarity and consistency about the pipeline. The process would ideally deliver:

1. The **business case**. In the first instance, a strategic case should outline the need for the project (its objectives), options for delivering it, impact, costs and the risks it might entail, with suitable independent challenge from outside the sponsoring Committee.
2. The **confirmed projects that are in the pipeline** through a suitable process in the States. That process should consider the budget envelope that is available.
3. The resulting **Agreed Infrastructure Pipeline** ('AIP') that would be taken forward with public knowledge of what was planned and when it will be progressed.
4. The **pipeline as a "live" document.** It can be updated on a rolling basis based on a new gap analysis and new business cases. This rolling pipeline does not change the projects that have been committed.

The whole process could be overseen by a team that is able to report transparently to political and non-political leaders alike, as well as the wider public.

In other jurisdictions, such as the UK, the process is overseen by an independent body who can stand back from the political cycle and help to reduce costs by supporting a consistent approach to projects and the pipeline. There is also important involvement from finance or treasury departments with all parts of the public sector feeding in new business cases. The objective of the process is to provide sufficient certainty that the necessary investment can be made in the supply chain (construction companies, materials needed as inputs, people with the right skills) such that the cost of delivery is minimised. If the pipeline is uncertain then businesses cannot plan and it is more expensive to then mobilise quickly when it is clear that a particular project will be allowed to proceed.

There are some differences between the process for infrastructure spending in Guernsey and processes adopted elsewhere. We note three:

1. **Longer term view:** planning focuses on the short- to medium-term and the priorities set within each political term. There is limited commitment to a longer-term 'guiding view' of the needs for the economy. For example, in the UK the NIC provides a 30-year view of infrastructure need. That can help to frame the shorter-term (parliament-by-parliament) debate.
2. **Benefits should be emphasised:** much of the debate and discussion can be about the costs. While this is an important consideration, it should also be set against the projected benefits. Again, in the UK the NIC seeks to clarify expected benefits (e.g. productivity, fairness) as well as the costs.
3. **Ensure public ability to monitor progress:** while progress is tracked well by officials and, on request, reported to Committees and the States, there is little published about

progress. In the UK, the Infrastructure and Projects Authority publishes its analysis of the 'national infrastructure and construction pipeline' including a spreadsheet of all major projects and their status for 10 years ahead, including the workforce requirements to deliver it.

The link between infrastructure spending and workforce is particularly important. The construction workforce may be a constraint on the ability of the Island to push forward with multiple infrastructure projects, particularly where it might coincide with high demand for private sector development. Increasing capacity in the construction sector is beyond the scope of this report, but remains a priority. Clearly signalling the medium- and long-term intentions of the portfolio so that providers (be they construction or other delivery agents) have an overview of what is upcoming is likely to help companies to plan their commitments more effectively and maximise the available capacity. Ensuring suitable housing and related measures is also important.

Housing

In Guernsey there is a very clear link between housing supply and the rest of the economy, including the ability to deliver other infrastructure projects where that might require an expansion of the construction workforce. That likely means housing affordability is more closely linked to GDP than in other countries. As such, housing supply should be viewed as critical to infrastructure delivery.

Housing is currently under-supplied in Guernsey. The waiting list for social rental housing suggests that total social housing stock needs to increase by about 10%. Furthermore, the 2024 Monitoring Report for the States' Strategic Housing Indicator[18] ('SSHI') identifies the need for an additional 673 units of affordable housing over the next five years.

One approach to better regulating housing supply – advocated by the 2004 Barker Review of Housing Supply[19] — links the rate of supply to measures of housing affordability: more supply is authorised/commissioned as affordability indicators (mainly earnings compared to housing costs) worsen. This provides one possible mechanism to judge and trigger suitable housing supply.

Regardless of the specific approach to housing, it is more generally important to provide greater reassurance about the pipeline of all projects.

All development of new affordable housing is managed by the GHA. The GHA is a housing association limited by guarantee and, in addition to its core function of managing and maintaining its existing stock, it seeks to deliver new homes against the Affordable Housing Indicator ('AHI').

[18] https://www.gov.gg/CHttpHandler.ashx?id=184607&p=0
[19] https://web.archive.org/web/20080727035230/http://www.hm-treasury.gov.uk/media/E/4/barker_review_execsum_91.pdf

The States-agreed AHI sets the number of social rental and partial ownership units that need to be created if Guernsey is to meet its housing needs over a five-year period (currently 2023 – 2027). The Affordable Housing Development Programme (mandated through the Committee *for* Employment & Social Security – 'ESS') seeks to meet this indicator, and one delivery body for this is the GHA. The GHA funds developments from both long-term borrowing (either from the States' Bond or via private borrowing) and capital grants (allocated through the States' capital prioritisation process).

The approval process for GHA developments is the GHA Board, then ESS and P&RC (the latter two in compliance with the AHI and the authorisation of the capital grant). Individual projects do not need approval from the States unless the capital grant to be made from the core Major Projects Portfolio is greater than P&RC's delegated authority.

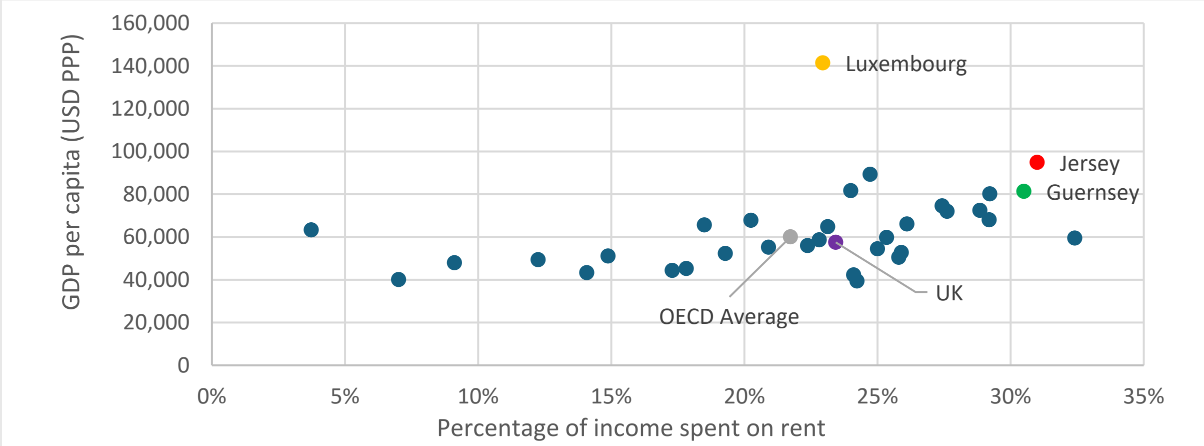
The GHA needs support from the States to increase its house-building efforts. That support should not detract from other infrastructure projects but should encompass how to finance new construction without endangering other infrastructure investment and how to match targets with need.

Box 1: Guernsey's housing issues

Although not directly part of the government's investment portfolio, investment in residential housing (particularly social housing) is a key issue for Guernsey. Like other rich countries without an easily accessible neighbor, the average person in Guernsey spends a high proportion of their income on housing.

Fig.13 - Rent (private and subsidised) as a percentage of net income versus income per capita, OECD.

Source: OECD, Guernsey Data and Analysis, Statistics Jersey

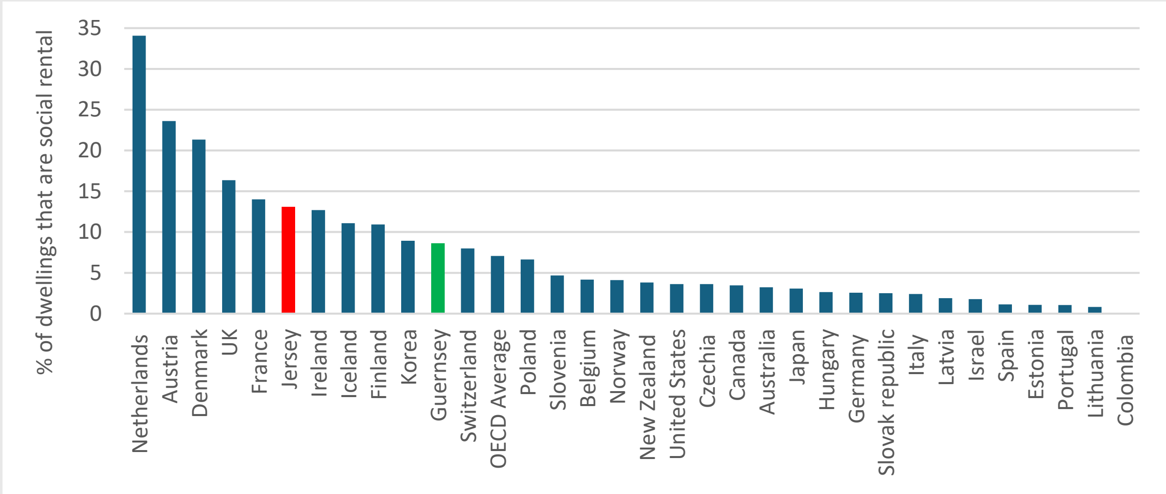


NB: The Guernsey comparator in Fig.12 reflects percentage of income spent on all housing costs (including rent, mortgage, maintenance, utilities etc.) rather than just rents as it is the only available comparator.

This raises significant issues for those on lower incomes as housing can effectively be unaffordable for important parts of the labour market, including key workers. In most countries this problem is at least partially ameliorated by the creation of a large stock of social housing that is ringfenced for those on lower incomes. Guernsey's social housing stock is small and so is arguably a constraint on the growth of the economy as labour shortages in key areas are more likely.

Fig.14 - Proportion of households in social housing, Guernsey, Jersey and OECD countries

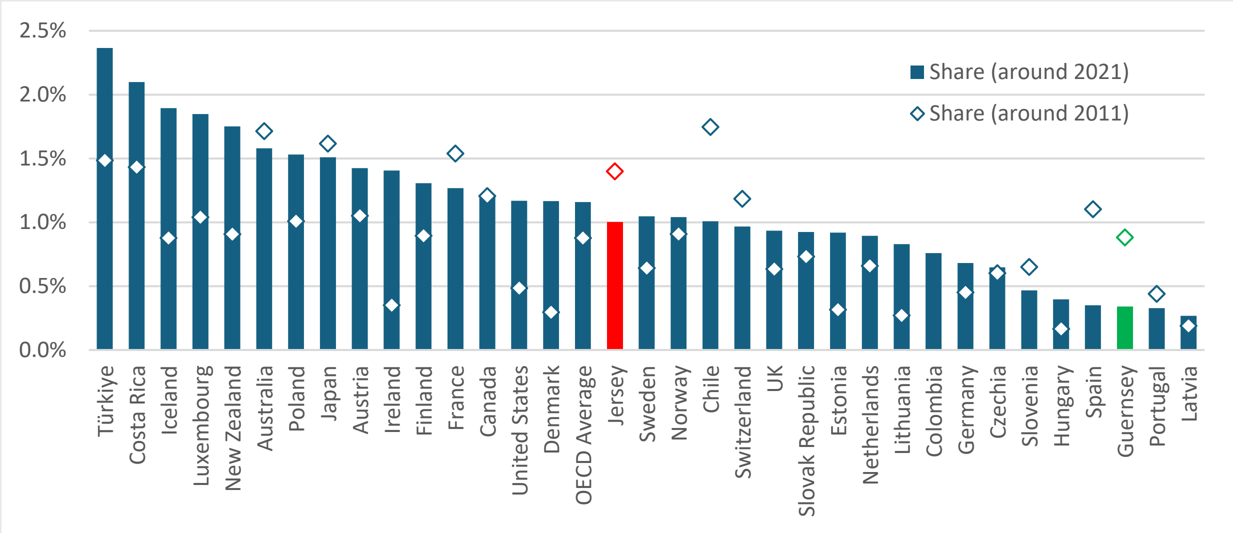
Sources: Guernsey Data and Analysis, Statistics Jersey, OECD



More generally, Guernsey's investment (both public and private) in housing in recent years has been well below its stated targets. Its current measure (the SSHI) shows a requirement for around 300 new dwellings per year (160 in the private sector and 140 affordable) over the five-year period from 2024 - 2028, but an average of only 110 a year have been built over the past five years.

Fig.15 - Housing construction - share of dwellings completed in the year, as % of total existing housing stock

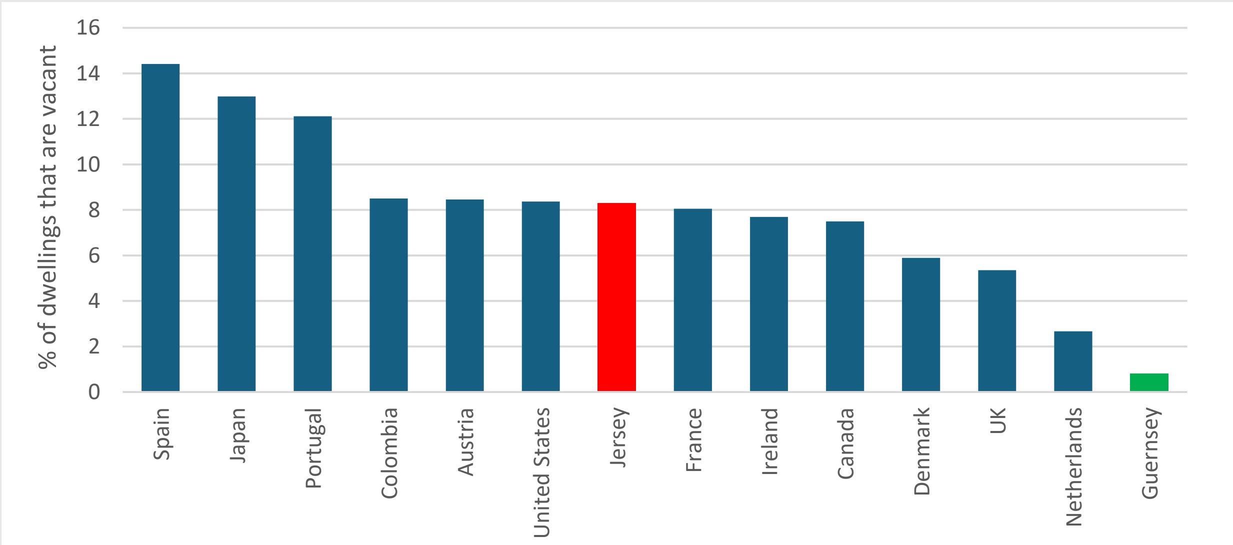
Source: Guernsey Data and Analysis, OECD, Jersey Fiscal Policy Panel Report



Although an indication of a well-utilised housing stock, Guernsey's very low vacancy rate may also be an indicator of excess demand.

Fig.16 - Vacant dwellings - percentage of total dwellings classed as vacant, OECD and selected countries

Sources: Guernsey Data and Analysis, Statistics Jersey, OECD



7. The States' financial reserves, investments and debt

The States currently holds financial and investment reserves totalling £1,553m (as at December 2023). These can be divided into three broad categories:

- The Core Investment Reserve (£169m at December 2023), which is intended to function as the States' 'sovereign wealth fund';
- The General Revenue Reserve (£497m at December 2023) which broadly speaking functions as the States' operating capital and includes the Guernsey Health Reserve and the residual proceeds of the Guernsey Bond. Some of this reserve is allocated for specific purposes.
- The Guernsey Insurance and Long-Term Care Insurance Funds (£898m at December 2023), which are specifically bound in legislation to support the provision of pensions, contributory benefits and Long-Term Care benefit respectively.

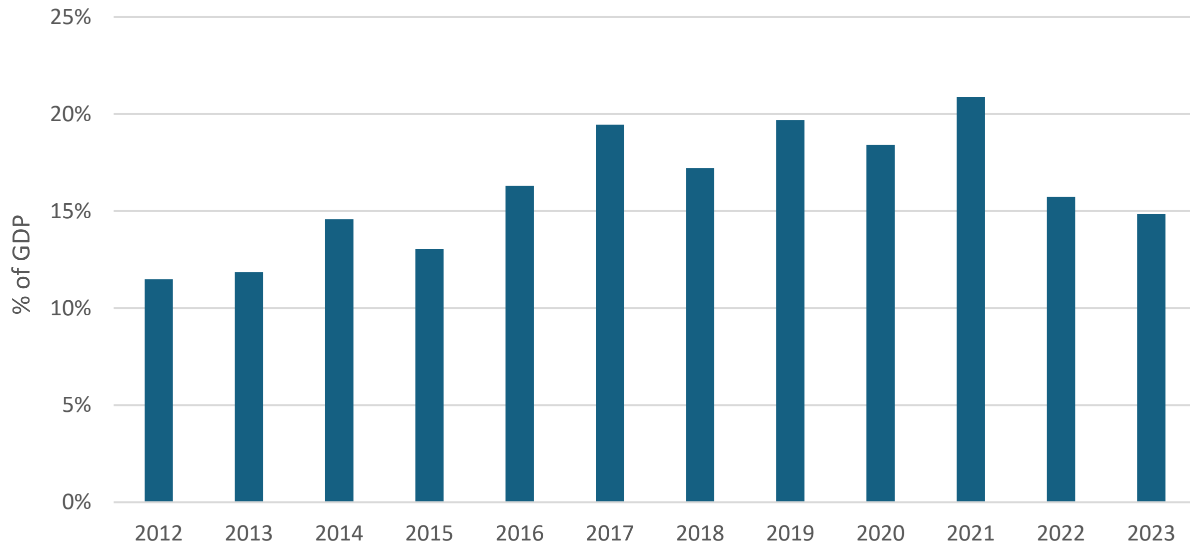
General Revenue Reserve

The General Revenue Reserve ('GRR') is used to support the States' short- to medium-term operating plans and can be made available to support capital investment. It was created in December 2020 to consolidate various earmarked funds into a simplified structure, incorporating the former Capital Reserve, the unspent balance of the debt issued in 2016 and other funds. In 2022 the Guernsey Health Reserve was also transferred to an earmarked reserve within the General Reserve.

The total closing balance of the reserve in 2023 was £497m, of which £26m was earmarked and not available for use. This leaves a balance of £471m which might be available for use from 2024 onwards, of which £105m is specifically ringfenced for use in supporting health provision.

The low levels of capital spending from 2014 onwards and two years of particularly low investment combined with strong asset growth in 2016 and 2017 (and to a lesser extent 2019 and 2021) have allowed for an expansion in what might be termed the States' 'usable funds'. More recently, high inflation and poor investment returns in 2022, and a worsening operational position, have eroded the real value of the reserve.

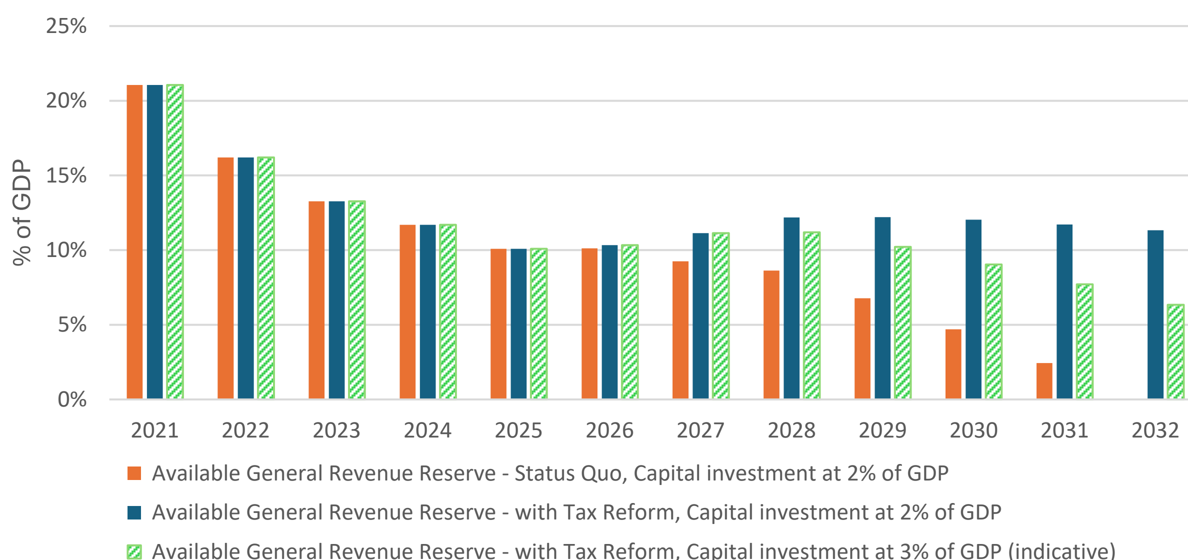
Fig.17 - General Revenue Reserve balance as % GDP



The reserves available, the returns they generate and the surpluses available are not sufficient to meet the States' current requirements. The below projections from the States' Major Projects Portfolio Review show that if the portfolio of investment continues as agreed, and reverts to an average level of investment of 2% of GDP from 2028, the available resources would be exhausted by 2032.

This downward trend in the value of the reserve is a classic symptom of an unsustainable fiscal path where depleting existing reserves and/or debt accumulation are used to plug a persistent gap between revenue and expenditure. Outside observers such as rating agencies will clearly see this trend, and their actions (e.g. lower credit ratings) are likely to accelerate it by increasing the cost of external finance.

Fig.18 - Projection of available reserves with and without tax reform and with capital investment at 2% and 3% of GDP[20]



With the inclusion of the States' agreed tax reforms from 2027 the projected position of the reserves is healthier, with the additional revenues stemming the rapid outflow of money from reserves. However, it is not sufficient to fully maintain the value of the available funds relative to GDP. If the States were to directly fund investment at 3% of GDP, further action would be needed.

Core Investment Reserve

The Core Investment Reserve ('CIR') is the equivalent of the States' 'sovereign wealth' fund. It is a long-term investment reserve which should only be made available for use in exceptional circumstances. It is not included in the projection of available funds as described in the Major Projects Portfolio Review.

The official policy is that this Reserve should hold a target balance of 100% of General Revenue income, but it is a long way short of this. At the end of 2023 it held £169m - less than a third of its target value.

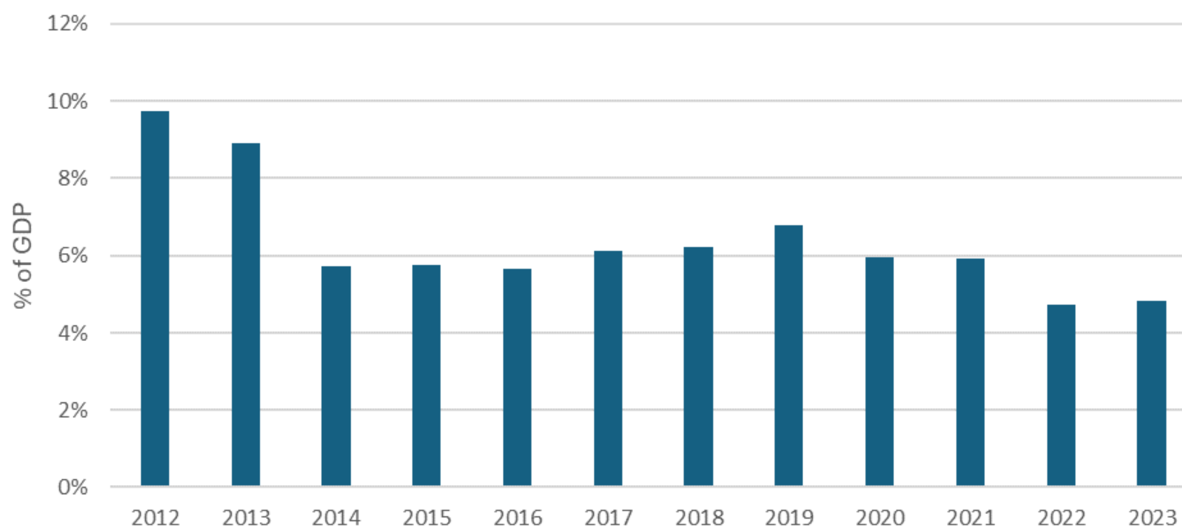
The CIR saw a significant drop in value in between 2012 - 2014 because part of the reserve (then known as the Contingency Reserve) was allocated to smooth the transition of the new corporate tax strategy following the implementation of Zero-10.

Since 2014 the value of the reserve relative to GDP has remained relatively stable. Much like the GRR, poor asset growth and high inflation in 2022 have reduced the relative value of the fund. A

[20] Major Projects Portfolio Review, dated 17 January 2025

portion of the reserves were also used to support the cost of economic support measures applied during the Covid-19 lockdowns.

Fig.19 - Core Investment Reserve balance as % GDP

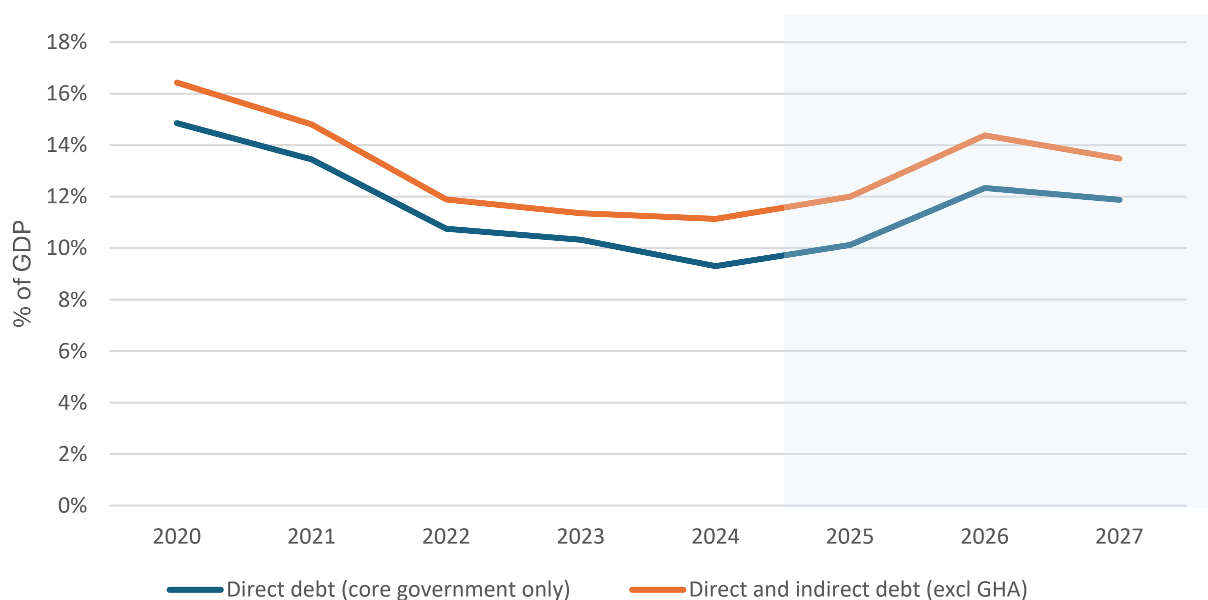


Given that the purpose of the fund is for exceptional events such as a significant problem in Guernsey's financial services industry, its current scale is substantially below what would be required to support the economy through such an event. In our last report we demonstrated how these exceptional events - when they have occurred in other small economies (such as Iceland and Cyprus) - require a buffer of around 30% to 60% of GDP in order to offset the fiscal costs of such an event.

General Revenue direct debt and contingent liabilities

The States held £340m of direct debt at the end of 2024; £330m in respect of the bond issue made in 2016, and £10m held on a rolling credit facility ('RCF') secured during the Covid-19 pandemic, which has subsequently been utilized to manage short-term debt positions. These have a current relative value of approximately 10% of GDP which is, in international terms, a very low level of debt but, combined with the steady reserve drawdown is indicative of an unsustainable path. Because no new debt has been issued over the last four years, a combination of the pay down of the RCF and the impact of higher than typical inflation in 2022 and 2023 have eroded the level of debt.

Fig.20 - Government debt as % of GDP[21]



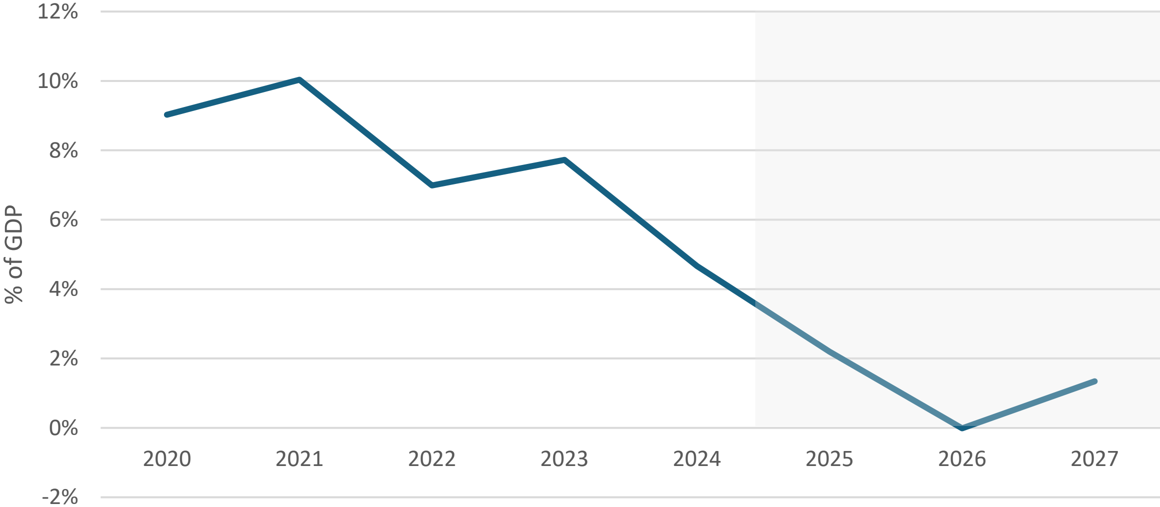
Looking forward, the stated intent is to borrow a further £155m to fund the current Major Projects Portfolio, increasing the peak debt position to a forecasted 12% of GDP. No assumptions have been made about further debt issue beyond the current portfolio, and as a result the debt position is forecast to erode relative to GDP over time.

The States also holds ultimate liability for debt for the wider accounting group. Incorporating the current indirect liabilities, the peak projected debt is expected to reach 14.4% of GDP. However, it is anticipated that both the GHA and Guernsey Electricity may need further borrowing to support major investment programmes and that these will need some form of guarantee by the States, which will increase debt levels further.

The States does not have longer-term debt projections, which likely reflects the medium-term nature of the current major projects planning cycle and the uncertainty over the financial position going forward.

[21] States of Guernsey Strategic Finance Team

Fig.21 - Net reserve balance as % of GDP (Core Investment plus General Revenue Reserves, less direct debt)



Comparing the States' direct debt to the value of the GRR and the CIR, the States currently holds a net reserve position of around 5% of GDP (excluding the hypothecated social security funds discussed later in this section which hold around 25% of GDP in reserve).

The anticipated additional borrowing to support the current Major Projects Portfolio is expected to reduce the net reserve position to approximately zero i.e. the States' financial assets held in these two funds will approximately equal the total direct debt held.

Guernsey Insurance Fund

The Guernsey Insurance Fund ('GIF') is a social insurance arrangement used to provide old age pensions, sickness and unemployment benefit among others. The last actuarial review of the GIF was undertaken as at 31 December 2019 which revealed that it would be exhausted by 2039 unless measures were taken to either increase the amount going in, or to reduce the level of benefits being paid out. The States' current target for the sustainability of GIF is a fund value equal to a multiple of two times annual expenditure at the end of the projection period.

Subsequently, the States agreed in principle to increase the contribution rates to GIF each year for 10 years to meet its sustainability target as shown in Fig.22. This will take the total contribution rate to GIF for an employed person from 9.75% in 2022 to 11.55% by 2031.

Fig.22 - Projected progress of the GIF from 2019 allowing for planned future contribution rate increases[22]

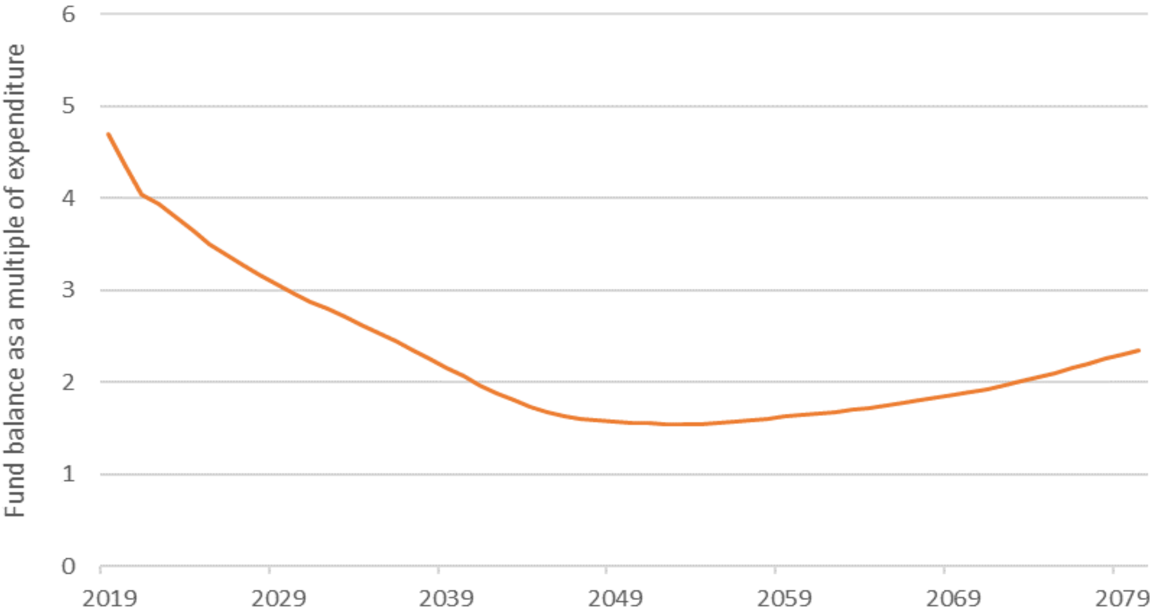


Fig.22 shows that the value of assets held in the GIF as a multiple of benefits expected to be paid out is projected to fall steadily until around 2049, after which it increases gradually until the end of the 60-year projection period.

However, recent analysis undertaken in relation to the Long-term Care Insurance Fund ('LTCIF') suggests that the financial position of the GIF may have worsened since the actuarial review, with the fund balance now expected to continue reducing until the end of the projection period. This suggests a total contribution rate for an employed person of above 11.55% would be required after 2031. This will be formally reviewed as part of the actuarial review due as at 31 December 2024. This is expected to be published later in 2025.

Long-term Care Insurance Fund

The LTCIF is a social insurance arrangement used solely for the provision of long-term residential and nursing care. The last formal actuarial review of the LTCIF was undertaken as at 31 December 2019[23] which revealed that it would be exhausted by 2053 unless measures were taken to either increase the amount going in or to reduce the level of benefits being paid out. The States' current target for the sustainability of the LTCIF is a fund value equal to a multiple of two times annual expenditure at the end of the projection period.

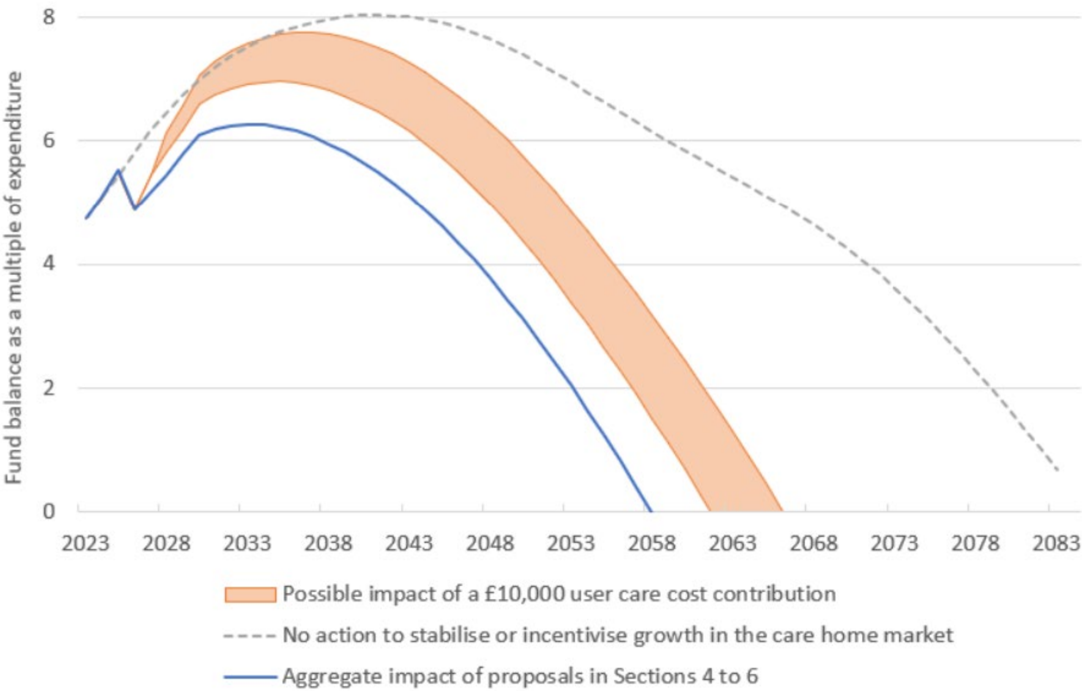
[22] GIF - Actuarial Review as at 31 December 2019 - GAD
[23] LTCIF - Actuarial Review as at 31 December 2019 - GAD

Subsequently, the States agreed in principle to increase the contribution rates to the LTCIF each year for four years to meet its sustainability target. This took the contribution rate for an employed person from 1.8% in 2021 to 2.2% in 2025.

A further interim actuarial review was undertaken as at 31 December 2022 as part of the States' wider considerations of the delivery of long-term care in the Bailiwick. This included a review of the underlying assumptions and allowed for the increase in contribution rates, concluding that the LTCIF is expected to be completely exhausted by around 2085.

The States has recently agreed proposals to amend the provisions of the LTCIF which will see it exhausted much sooner, by the mid-2060s as illustrated in Fig.23.

Fig.23 - Projected progress of the LTCIF from 2022 allowing for approved changes to its provisions[24]



Although not suggested as a course of action, the Policy Letter presented to the States suggests that to meet its sustainability target at the end of the projection period following the approval of the change to the provisions, an increase in the contribution rate for an employed person of between 55-70 basis points would be required from 2026. In 2024 terms that is an estimated revenue requirement of around £9m to £12m.

A formal actuarial review of the LTCIF is due to be undertaken as at 31 December 2024.

[24] Billet d'Etat V of 2025, Article 3, The Need to Stabilise the Private Care Home Market and Incentivise Growth to Meet Demand

8. Overall Fiscal Sustainability

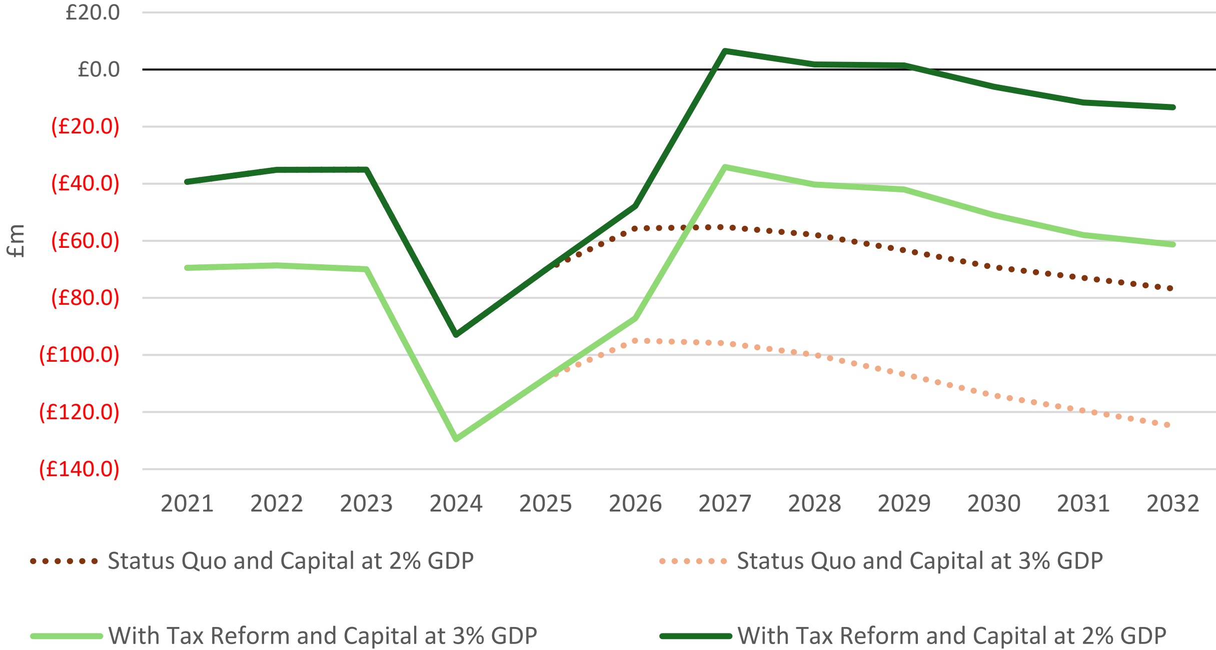
The Panel's previous report (www.gov.gg/fiscalpolicypanel), which reviewed the 2023 Funding & Investment Plan, considered the States' overall fiscal stability in more detail. While it is not directly within the Panel's brief for this year, it is evident that fiscal issues have play a significant role in the progression of the Major Projects Portfolio and management of the States' debt and asset portfolio.

We highlighted in our last report that the States' current revenue base was not sufficient to support both its current profile of services and the amount it should be investing in Guernsey's infrastructure, and that position remains unchanged. Without the delivery of additional revenues via the tax reforms agreed in the 2025 Budget (with projected implementation in 2027/8), the States' finances are unsustainable.

Successful implementation of the tax reforms is projected to be able to sustain capital investment directly from the Government of around 2% of GDP. Having reviewed the available evidence the Panel recommends that total investment in infrastructure should be closer to 3% of GDP, noting that some of this investment in critical infrastructure is delivered via the States' trading assets and financially supported, at least in part, by the commercial activity of those entities, and is therefore not directly (or entirely) supported by the tax base. Recent history suggests that, excluding housing, these entities typically invest between 0.5% and 1% of GDP in capital projects.

We therefore recommend that the States plan for an average level of capital spend directly from government resources averaging 3% of GDP – this would include taxpayer-financed investment in critical infrastructure from States' trading assets, which is a slightly wider definition of capital spend than is used in the current Fiscal Policy Framework. The States will need more resources to sit sustainably within the recommended range, but having implemented tax reforms, further measures needed to achieve this will be more moderate.

Fig.24 – States' deficit after capital investment at 2% and 3% of GDP, with and without tax reforms[25]



9. Recommendations

The Panel's recommendations focus on maintaining a permanent fiscal balance by ensuring that revenue, spending, infrastructure investment and reserves are maintained over time without resorting to emergency measures or the accumulation of unsustainable debt.

- **Revenue:** revenues in recent years have proved insufficient to support the Panel's definition of maintaining permanent fiscal balance. Tax reforms currently proposed (but not yet implemented) are an important step towards long-term fiscal sustainability, including the ability to fund Routine Capital and Major Projects Portfolios, *if they are implemented*. The Panel recommends the States take action to ensure revenue streams are sufficient to meet the needs of day-to-day service provision, fully fund the capital programmes and maintain reserves relative to their projected liabilities.

- **Spending:** As a share of GDP, Guernsey spends less on most domains of public services than comparable jurisdictions. Only on health services does Guernsey's spending match the OECD average. This is indicative of a lean public sector. However, Guernsey's older age dependency ratio is already higher than the OECD average and expected to rise through 2050. We therefore expect an increase in associated costs around health and social care.

[25] States of Guernsey Strategic Finance Team

The Panel notes that these are foreseeable and fiscal prudence requires early action to plan for these, including the agreed increased contributions to the GIF.

- **Reserves:** Guernsey's reserves and funds are under strain. The status quo on taxes and capital investment at 2% of GDP would see the available GRR depleted by 2032. This is against the Panel's preferred target of 3% of GDP for investment. The CIR is also significantly below (less than one third of) its target value. Research suggests that a buffer of 30% - 60% of GDP would be needed for the CIR to properly serve as protection against a severe economic shock. Finally, actuarial reviews of the GIF and LTCIF reveal unsustainable trajectories for both. Proposals to increase contributions – if delivered – would help, but may not be of sufficient magnitude to ensure the funds are able to meet growing liabilities.

- **Infrastructure investment:** Chronic underinvestment in Guernsey's public infrastructure is an increasingly binding constraint on growth, fiscal sustainability and living standards. The Panel recommends urgent action to ensure the pipeline of projects is delivered as smoothly as possible and with minimum delays. The Panel's preferred target for infrastructure investment would be to average 3% of GDP over the medium- to long-term. Careful consideration should be given to managing the pipeline and coordinating projects with capacity in financing, construction and planning. A concerted effort is required to minimise the stop-start processes and frequent revisions to projects that delay delivery, increase uncertainty and drive-up costs.

- **Taking a longer-term view of infrastructure:** The Panel endorses taking a longer-term strategic approach to planning and delivering key infrastructure, including housing. In addition to better initial planning for projects, this could send a clear signal to the construction sector that increasing capacity would be a 'safe bet'.

- **Clearly articulate the benefits of infrastructure investment:** Much of the debate around infrastructure investment focuses on up-front costs of delivery. This is of course important, but it is equally important to articulate the economic and welfare benefits associated with better infrastructure, and to be honest about the 'do nothing' counterfactual: that is, the costs imposed on people and the economy due to obsolescence and crumbling infrastructure.

- **Ensure effective oversight and regulation of States' trading entities:** Much of Guernsey's critical infrastructure formally 'sits' on the balance sheets of quasi arm's-length companies. Effective oversight and regulation is required to ensure that these infrastructure assets are maintained over time to avoid the need for public bailouts in the face of crises. Where investments by these entities constitutes core infrastructure for the Island, the public contribution towards capital spend by these entities could count towards meeting the 3% target.

10. APPENDIX 1

Terms of Reference for Fiscal Panel

a) To examine the matter of sustainable infrastructure investment including:

- An outline of the economic principles behind the need to invest in public infrastructure;
- To outline the relationship between infrastructure investment and its importance in achieving permanent fiscal balance;
- To consider the definition of infrastructure investment within the boundaries of the Fiscal Policy Framework ('the Framework') and whether this should be constrained to investment directly under the States' control or extended to cover investment made via the States' controlled ports and utilities, or further still, extended to consider investment made by privately owned regulated entities in public goods and networks (such as the telecommunications companies);
- To consider, with reference to international norms and the practice in other small island jurisdictions:
    - Whether it is appropriate for Guernsey to include a clearly defined target for infrastructure investment within the Framework, or whether it is more appropriate for the level of spend to be guided by the needs identified via the capital programme; and
    - If the Framework should include a target, or guide level of spend, at what level might be appropriate given Guernsey's size, capacity for large scale developments and fiscal constraints.

b) To consider the role of cash and investment holdings in achieving sustainability, and specifically the role of the Core Investment Reserve including:

- The range of international practice with regard to the holding of government reserves; and
- What is an appropriate level of long-term investment reserves for Guernsey to target.