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A small island territory moving down the 'development ladder'? A case study of Jersey

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Abstract: The small island economy of Jersey in the Channel Islands is one of the world's most economically successful offshore financial centres. Jersey has long demonstrated its ability to respond to changing economic circumstances as it has adopted policies conducive to good economic, social, political and environmental governance. Over the last twenty years, there have been a growing number of challenges to the island's economic resilience. Foremost among these have been regulatory threats to the finance industry; the Global Financial Crisis (GFC) and its aftermath; faltering growth in productivity; growing expectations of increased and better public service provision; and weak political governance. In line with the literature that argues there is a three-way taxonomy of small-island socioeconomic formations, comprising MIRAB, PROFIT and SITE types, this paper considers the recent challenges to Jersey's economic resilience and its place on the 'development ladder'. The paper concludes that Jersey's experiences offers salient warnings to other successful small jurisdictions.

Keywords: offshore finance centres; economic development; small states; island economies

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Introduction

Since the Global Financial Crisis (GFC) of 2007-8, Offshore Financial Centres (OFCs) have faced unprecedented levels of attention from international organisations such as the OECD and the media. Academics have contributed to the debate on technical aspects of how tax evasion and regulation is allegedly facilitated by OFCs and the morality of tax avoidance (e.g. Elsayyad and Konrad, 2012; Shaxson, 2012; Young, 2013, 2016) but the focus on the rights and wrongs of offshore finance has overshadowed a far more interesting, yet unexplored line of enquiry, about what has been going on 'under the bonnet' in OFCs.

Invariably, OFCs are to be found in small or 'microstate' jurisdictions. Warrington (1994, p. 4) proposed that a microstate could be defined in terms of population, geographical area and economic activity but defining precisely what constitutes a microstate has become something of a challenge for academics (e.g. Armstrong and Read, 2002a, 2002b; Baldacchino, 1998; Bray, 1987; Srinivasan, 1986; Sutton and Payne, 1993; Taylor, 1969). Some of the definitional problems stem from disagreement about how to quantify the characteristics of a microstate, e.g. does the population of a microstate equate to 100,000, 500,000 or 1 million inhabitants, and how does a microstate differ from a small state, if at all? There are qualitative challenges as well. Smallness might be viewed as a "perceptual problem" (Amstrup, 1976, p. 166) or it could be "merely a frame of mind, a subjective condition which pervades the mind-set of the actor, thus moulding horizons and agendas for action and perception" (Baldacchino, 1993, p. 159). Oest and Wivel (2010, p. 434) go as far to comment that "a microstate is a state that is always the weak state in an asymmetric relationship when interacting with another state at the global, regional or sub-regional levels, unless dealing with other microstates".

The small island economy of Jersey in the Channel Islands has all the preconditions to become a microstate, but is a self-governing dependency of the UK which is responsible for Jersey's international affairs and defence. It is also one of the most economically successful OFCs in the world. The total resident population of Jersey at the time of the last census in 2011 was 97,857 and its geographical land area is 120 km^2 (45.5 square miles). For the first half of the twentieth century, Jersey's economy was dominated by agriculture, then tourism. By the end of the 1960s, the tourism industry contributed almost half of Gross Domestic Product (Powell, 1971, p. 15), but following the growth of the Euromarket from the 1960s, Jersey quickly became established as an OFC. By the mid-1970s, the economy was well on the way to becoming a global level OFC (Hampton, 1996) and finance soon became the island's main driver of economic growth (Table 1). By 2000, financial services accounted for over half of total Gross Value Added (GVA); Jersey held bank deposits of over £118 billion and £91 billion was managed in offshore funds (States of Jersey Statistics Unit, 2008, pp. 18-19).

Table 1: Estimated contribution of the 'primary sectors' to Jersey's GDP, 1970-1994.

	Estimated contribution as a percentage of GDP			
Sector	*1970*	*1980*	*1990*	*1994*
Finance	15	26	45	54
Tourism	45	38	29	25
Investment holders	25	23	19	14
Agriculture	8	6	5	5
Light industry	7	7	2	2
Total	100	100	100	100

Source: Hampton (1996, p. 141).

It was only at the start of the twenty first century that the balancing act of a "managed dependency" (Mannin, 2006, p. 389) became more difficult, largely as a result of external pressures from the OECD and EU to regulate so-called 'tax havens' and internal pressures on Jersey to reform. At the same time, the expansion associated with the growth in financial services led to increasing unease in the local community and the development of a strong sentiment against the consequences of this growth such as building in the countryside, a growth in population and the consequent increase in the provision, and hence cost, of government services (Mitchell, Sikka, Christensen, Morris and Filling 2002, p. 25; Sikka, 2003, p. 381; Policy and Resources Committee, 2001).

Work by Briguglio, Cordina, Farrugia and Vella (2005, 2009) on economic vulnerability and economic resilience suggests that small, often island jurisdictions, are more likely to be exposed to external shocks with a high degree of economic openness; a high degree of export concentration; and a high dependence on strategic imports such as fuel and food. Such jurisdictions can absorb and counteract the effects of economic shocks if they adopt policies conducive to good economic, social, political and environmental governance. Baldacchino and Bertram (2009, p. 147) have critiqued Briguglio's (1995) 'vulnerability paradigm' and in so doing, note "there is no well-established empirical basis for claiming economic vulnerability". Their preferred paradigm to examine the performance of small economies is to consider strategic flexibility. Until the GFC, on both grounds of strategic flexibility and economic resilience, Jersey has historically met numerous challenges (Entwistle and Oliver, 2015). In recent years, however, there have been a number of challenges which have given cause for concern, namely, the growing threats to the finance industry and its profitability; the limited diversification of the economy; growing expectations of increased and better public service provision; and weak political governance.

With few exceptions, there has been little academic work on Jersey's economy over the last two decades (Christensen and Hampton, 1999; Hampton and Christensen 2011; Entwistle and Oliver, 2015; Le Rendu, 2004). To account for developments, this article draws from a number of published reports, statistical data and the author's experience working as an adviser to one of the island's Scrutiny Panels, to assess economic developments in Jersey since 2000. The article is divided as follows. First, it considers Jersey's place in the taxonomy of small states. The article then turns to consider the challenges to resilience before and after the GFC, before exploring how Jersey has been weakened by both endogenous and exogenous factors. It concludes that Jersey's experience offers salient lessons for other small states who wish to avoid going down the 'development ladder'.

The taxonomy of small states and its applicability to Jersey

Examining small jurisdictions has proved problematical for many economists and political scientists. On the one hand, classical economic theory would suggest that small countries suffer from a lack of economies of scale and have small domestic markets, both of which are a handicap for economic development (e.g. Briguglio, 1995; Jahan and Wang, 2013, p. 45). On the other hand, small countries are often more open to international trade and recognise that greater specialisation is vital for them to succeed in increasingly competitive world markets. It is little wonder that for many economists, Baldacchino's (1993, p. 35) observation of small states probably endures:

> They fail to meet the credential of the closed-economy basis of standard development models on every count. Open-economy elements such as trade, capital flow, migration and exposure to world prices are not an annexe but rather constitute the main economics flows of such small states.

Over the last thirty years, work by academics on the political economy of small island economies has refined our thinking. In particular, the work of Bertram and Watters (1985, 1986), Armstrong and Read (1998, 2002a, 2002b), Baldacchino (1998, 2000), Baldacchino and Milne (2000) and Prasad (2004) *inter alia*, has challenged many of the long held assumptions of economists. The evidence they present has suggested that small states display stronger economic performance than traditional development economics would suggest; that small dependent territories outperform sovereign small states and that small island economies outperform landlocked ones.

In the mid-1980s, Bertram and Watters (1985, 1986) developed the MIRAB model to account for modern economic growth in five Pacific island jurisdictions. MIRAB sought to explain the economic development of these islands based on a mix of migration (MI), remittances (R), aid (A) and bureaucracy (B). These economies were sustained by a process of "negative feedback loops which kept the aid flowing, the migrants moving, the bureaucrats operating and the remittance networks alive, while the islanders' society and culture were reproduced through time and across transnational space" (Bertram, 2006, p. 2). In this framework, small islands do not suffer from vulnerability and can exploit niches of opportunity in the global economy. Moreover, it also suggests that market capitalism has a limited role to play in the economy, except when "introduced as a deliberate act of social engineering by policymakers" (Bertram 1986, p. 809). The economies of these islands could instead be developed by the expansion of the public sector, which required ever increasing amounts of government expenditure. The rise in rent seeking behaviour from civil servants, landowners and local governments, was a logical concomitant of the growth in public expenditure and led Brookfield (1986; quoted in Connell 1988, p. 81) to quip that MIRAB should be MIRAGE (where GE represents government expenditure).

The MIRAB model has been applied to other small countries in the developing world (e.g. Poirine, 1994) and has stood the test of time but with some minor adjustments and modification, leading Bertram to comment on his five Pacific case studies in 1999 that the "empirical record casts substantial doubt on the conventional wisdom that regards unrequited transfers as an unsustainable basis for material welfare" (Bertram 1999, p. 111). One of the central criticisms of MIRAB is that it does not always apply to developing and developed small island economies that exhibit a more sophisticated form of economic progress (McElroy, 2006; Oberst and McElroy, 2007). This had led to two alternative taxonomies to be considered: PROFIT and SITE.

In Baldacchino's PROFIT model, the focus is on P (people considerations); R (resource management); O (overseas engagement); FI (finance, insurance and taxation); and T (transportation). This model stresses the political/jurisdictional dimension rather than purely the economic, so that the "political economy of success" extends to "discretion over taxation and offshore finance ... language policy, shipping registration and property ownership" (Baldacchino 2006, p. 50). PROFIT economies would be more interested in:

> … a shrewd immigration and cyclical migration policy; engaging in tough external negotiations concerning the use of local mineral, natural, political and other imaginative resources; securing and controlling viable means of transportation; and luring foreign direct investment via very low/no tax regimes (Baldacchino, 2006, p. 54).

However, PROFIT does not encompass tourism, which for small island economies can be an important way to escape a MIRAB structure (e.g. Treadgold, 1999, who discusses the example of Norfolk Island). McElroy (2006) suggests that there is a group of small island tourist economies ('SITEs') who enjoy high rates of growth, high life expectancy, and lower infant mortality rates which approach the most advanced continental societies. To be sure, there are some SITEs which exhibit MIRAB characteristics and a third group of islands which fall between the most and least developed. For Bertram (2006, p. 6), this suggests a new taxonomy for about 50 small islands with considerable overlap between SITEs and PROFITs and a "rich research agenda" to be explored addressing questions such as "how many of the PROFIT economies, for example, were previously MIRAB or SITE structures? How many SITEs started out as PROFITs or MIRABs? What common characteristics predispose an island economy to one or other of these structures?".

It is clear that, over time, various island states and territories have been able to demonstrate the characteristics of innovation, adaptation and change in response to numerous challenges and to compete effectively, both with other small or microstate jurisdictions and with larger jurisdictions that have greater capacity and resources (Baldacchino, 2011). In other words, they have managed to climb up the development ladder (Bertram and Poirine, 2007, p. 336, 360). Jersey is no exception to this: its ability to respond to changing circumstances is graphically illustrated by the historical transition of the Channel Islands' main industries, initially from cod fishing and knitting in the 17th century to ship building and agriculture in the 18th century (Ommer, 1991; Podger, 1962; Syvret and Stevens, 1998), then in the 19th century to tourism and, nowadays, international finance.

Although it was never a MIRAB, Jersey went through a SITE structure on its way to becoming a PROFIT economy. In this transition, Jersey has long enjoyed the characteristics of a 'free-riding' economy "in the context of (at times deliberate) oversight by the larger, metropolitan party [London, in Jersey's case], crafting in the outcome some kind of regulatory legitimacy" (Baldacchino, 2006, p. 50). Nevertheless, the regulatory legitimacy required careful political and economic management which avoided upsetting the metropolitan power and stopping short of full independence, while negotiating access to spoils within a larger jurisdictional framework. This frequently required Jersey to somehow manage its dependency:

> The trick, therefore, is to maintain the image/ reality of internal stability, economic prosperity and political autonomy: to manage dependency in the face of the uncertainties of global financial capital and the competition from other OFCs offering similar advantages. In effect, managed dependency is only successful if change is both recognised and responded to (Mannin, 2006, p. 389).

The structure of government, which enabled Jersey to manage its dependency, has confounded some commentators (e.g. Royal Commission on the Constitution 1973, p. 441). Although it is a small territory, its approach to governance is complex and cannot be understood without reference to its history (Le Herissier, 1998; Mannin, 2006; Le Feuvre, 1993). Jersey's allegiance to the Crown in 1204 enabled it to develop and maintain an arms-length relationship with the United Kingdom and maintain a high degree of internal autonomy. It was bolstered by a series of affirmations from the Crown confirming the Island's customs, traditions and domestic autonomy. The main point of contact was with the Crown in Council: the Crown acting through the Privy Council. However, this domestic autonomy, particularly in the area of financial autonomy, gradually came under pressure as a result of the growth of supra-national institutions such as the European Union (EU) and the Organisation for Economic Co-operation and Development (OECD).

One of the characteristics of Jersey's political system is evidenced in the Parish system, which has been the cornerstone of the organisation of Jersey Government. There has been a very long established tradition that parishioners are elected into positions on an honorary basis to perform work on behalf of the Parish. Over the centuries the Parishes accumulated very important powers and roles in respect of welfare, roads, education, and other matters. Kelleher (1994) has argued that the immigration into the island from the middle of the 19th century had a dramatic impact on the social and political structure of the urban areas of the island, particularly St. Helier, the capital. There was a very determined fight back from the rural areas to retain their traditional political and social institutions and culture and this meant that the rural areas saw the Parishes as very much the symbol and the centre of their power. Inevitably, pressures built up for reform but there remained a very strong clash between the urban view of how reform should be handled as opposed to the rural view, which was that Jersey's institutions had to be preserved and should not succumb to external pressures. The institutions were in essence a symbol of the island's high degree of independence and to interfere with the institutions was to interfere with the perceived independence.

The emergence of vulnerabilities

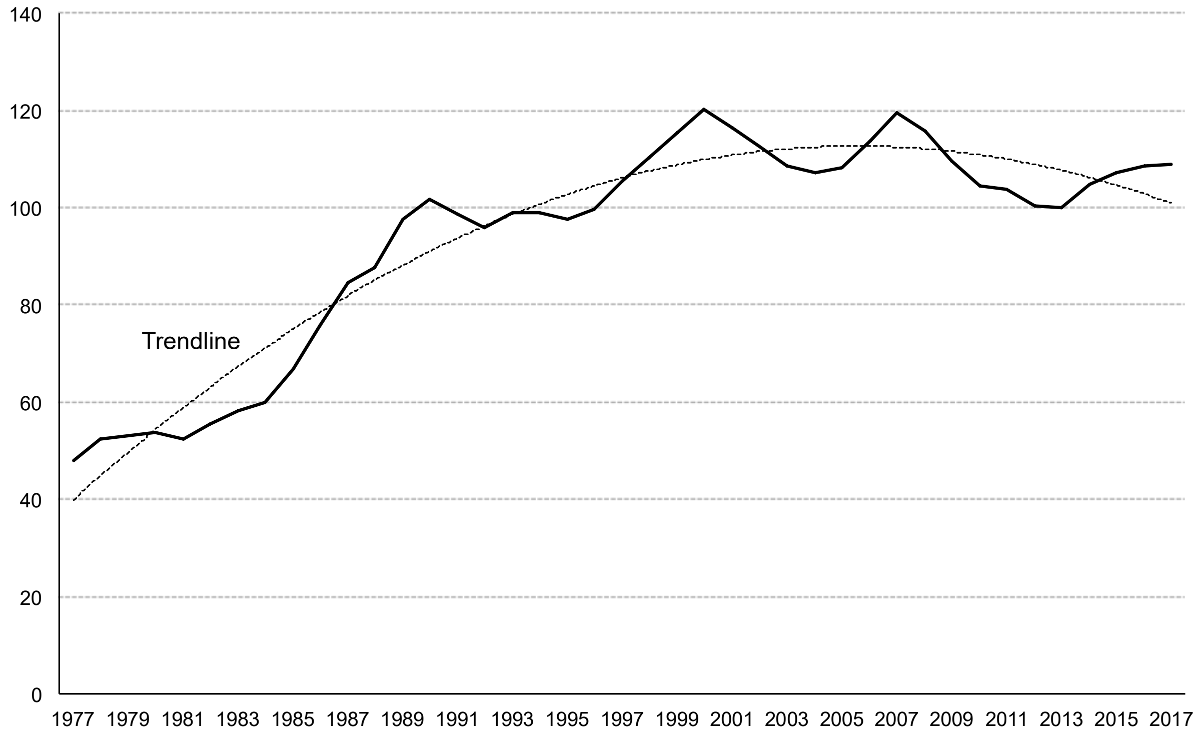
In the official narrative of the Jersey OFC, the story is told that Jersey showed great foresight and leadership and actively created the OFC from the early 1960s. However, this interpretation has not gone unchallenged and others have argued that the emerging offshore centre was driven by international financial capital and merchant banks set up on the island to service certain wealthy customers (e.g. Hampton, 1996). The corollary of this argument is that what then followed was a 'capture of the state'. This argument, associated with Christensen and Hampton (1999), contends that the island's largest industry not only dominated the local economy but also effectively 'captured' the Jersey government so that the interests of the financial sector tended to dominate the local political economy. Their central charge is that:

> As the OFC developed in Jersey during the 1970s and 1980s, its dynamism was such that it rapidly became the dominant industrial sector, and ultimately gained control of the island's political economy, thereby acting as a 'cuckoo in the nest' (Christensen and Hampton, 1999, p. 186).

Jersey has followed a similar pattern to other developed countries and increased levels of public expenditure on an annual basis. Unlike most countries, it was almost unique in managing to run annual budget surpluses because of the success of financial services and had a Strategic Reserve (referred to in the island as the 'rainy day fund'), which was set up in 1967. This allowed the island to have the best of both worlds: low taxes with West European environmental standards and robust public services. To be sure, as Christensen and Hampton have suggested, there has at times been an uneasy relationship between the financial services industry and more traditional sectors of Jersey's economy. However, politicians have successfully countered any criticism made of the finance sector by pointing to the considerable wealth it has brought to the island and its contribution, through the tax system, to pay for a range of social services. If the State was captured, so too was the rest of the population who were the recipients of the spoils of this positive fiscal situation and complicit in its presence. Yet, the successes of Jersey's PROFIT economy, and the political and economic structure which have supported them, have become increasingly vulnerable. It is to these that we now turn.

Jersey's growth transition over the last forty years is illustrated in Figure 1. Considerable caution should be attached to data points prior to 1998, as it was only since then that data was compiled according to international standards. Figure 1 illustrates the shift from low value added activities (e.g. tourism and agriculture) to high value added activities (financial services). As can been seen from the trend line, the impact of this transition has diminished over the last twenty years.

Figure 1: Real GVA, 1977-2017 (2013 = 100).



Source: Statistics Jersey and Economics Unit.

Note: Data on Jersey's economy has only been compiled in accordance with the United Nations System of National Accounts and the guidelines of the US Economics and Statistics Administration since 2004 and macroeconomic estimates such as GVA have been produced back to 1998 by Statistics Jersey. Data prior to this has been supplied by the Economics Unit.

The challenges to Jersey's economic resilience can be traced to the early 2000s when the high rates of economic growth that the island had experienced since the 1970s were checked by a sharp fall in GVA. Between 2001 and 2004, GVA in the finance sector fell by 17 per cent and total GVA fell by 11 per cent. Whilst economic growth did return by 2005 (see Figure 1), there were some significant storm clouds gathering which originated from external regulatory challenges.

OFCs initially managed to resist the increasing attention placed on them by the OECD in 1998 (Sanders, 2002; Shaxson, 2012, pp. 193-206; Vlcek, 2007). Jersey, along with the other Crown Dependencies, voluntarily committed to abide to the Code of Conduct issued by the European Council of Economics and Finance Ministers (ECOFIN) in 1999. ECOFIN's Code of Conduct on Business Taxation identified that Jersey's existing corporate tax regime was deemed harmful to the Single Market because it offered beneficial tax arrangements to non-residents, which were denied to residents. Jersey had to make changes to its tax system and planned to do so by 2009 when it intended to move away from a zero per cent corporate tax rate for offshore companies and 20 per cent rate for locally owned ones, to a single rate of zero per cent for all but some banks, trust advisory services and entities providing fund functionary services, which would pay 10 per cent. Companies could no longer be incorporated in Jersey as 'exempt' companies by paying a £600 per annum exempt fee (and thus avoid corporation tax); instead they were brought into the zero tax rate. Utility companies, rental income and property development profits would continue to be charged at the standard income tax rate of 20 per cent. It was estimated that the move to this new scheme, known as 'zero-ten', would reduce annual tax revenue by between £80 million to £100 million a year. To put that into context, in the early-2000s, total net revenue expenditure (i.e. expenditure to allow government departments to function) was around £400 million annually. The projected deficits from 2009/10 because of 'zero-ten' afforded Jersey a valuable opportunity to pursue broader reform on five fronts during the rest of the 2000s. As will be discussed, not all of these were successfully implemented.

From the mid-1990s until 2001, there was strong growth in real expenditure of 4 per cent per annum. This was a period of pro-cyclical fiscal policy, boosting demand further when the economy was growing strongly in real terms. Concomitantly, a whole series of government overspends on projects, and a perception that the public service was overstaffed or at least inefficient in how it operated, led to calls for more control of the growth of public expenditure. To try and tackle the growth in expenditure in government departments, a 'fundamental spending review' (FSR) was initiated in 2004. The objective was to identify spending and service reductions which could fund areas of necessary growth in public services and public spending within a period of fiscal restraint. In May 2004, the States Assembly agreed a voluntary initiative and promised transformative changes to the public sector. The aggregate annually recurring savings forecast to have been achieved by the end of 2008 was calculated at £36 million. However, as part of a series of reports into a review of the effectiveness and efficiency of Jersey's expenditure, the Comptroller and Auditor General (2008) identified that, of the total annual recurring savings said to have arisen from the FSR process, only £13.5 million represented an actual reduction in expenditure.

Despite the relative lack of success reducing expenditure following the FSR and the changes about to be undertaken to the corporate tax system, politicians did not appear alarmed because they assumed that there would be both strong growth in financial services and increases in revenue income. A year after the FSR, the States Assembly had agreed to set up a Stabilisation Fund which was designed to make fiscal policy more countercyclical and create a more stable economic environment with low inflation in Jersey. Funds would be paid into the Stabilisation Fund and a newly formed Fiscal Policy Panel (FPP), comprised of three leading economists, would publish an annual report on the state of the economy and recommend whether the Government of Jersey should run a surplus or a deficit and whether funds could be withdrawn from or paid into the Fund. This form of fiscal sub-contracting to an independent body was quickly put to the test.

Concerns continued to be expressed about several issues surrounding Jersey's public finances. In 2007, the Corporate Services Scrutiny Panel became uneasy about the funding pressures facing the Council of Ministers, particularly in light of the Council's overriding principle of ensuring that there would be no structural deficit over the period of the Government of Jersey's Strategic Plan for 2005-10 (States of Jersey 2004). In the early part of 2007, the Panel was presented with forecasts which showed a significant deficit in 2011 between £23m and as much as £58m, if inflation was worse than expected (Corporate Services Scrutiny Panel, 2008). The FPP also expressed concerns about Jersey's fiscal situation and warned in its September 2008 report of a deteriorating fiscal position. It pointed to the combination of spending pressures – including public sector pay – and the threat of slower growth in income tax receipts which could create structural problems within the island's finances. Their calculations showed "significant deficits…in 2010-2013 that are likely to be at least partly structural and require policies to address them" (Fiscal Policy Panel, 2008a, p. 36).

Politicians did not heed this advice and, following a debate on the Business Plan in the States Assembly, approved an additional £10m of expenditure per annum. In a further comment in November 2008, the FPP noted that the new items were "largely structural in nature" and hinted that there was now an increased risk of a medium-term deterioration in the island's finances (Fiscal Policy Panel, 2008b, p. 9). The 2009 Budget contained forecasts that revenue and expenditure would broadly balance from 2010 onwards but the FPP drew attention to the income forecasts, commenting that "there is a risk that rather more [expected income] proves to be cyclical as a result of recent strong economic growth, and rather less proves to be structural and thus sustainable, than the Treasury department has assumed" (Fiscal Policy Panel, 2008b, p. 8).

The deteriorating fiscal situation was masked by the numerous funds which Jersey could draw on, but the onset of the Global Financial Crisis in 2008 exposed more significant challenges. Between 2008 and 2013, GVA in the finance sector fell by 31 per cent and total GVA fell by 20 per cent. Unemployment, which prior to the GFC had been a few hundred, rose to almost 2,000 by early 2013. This was in part due to job losses in financial services, particularly banking, but also because of the removal of Low Value Consignment Relief (LVCR) in April 2012. LVCR allowed exporters to avoid paying VAT on goods shipped to mainland Britain for items under £15 and employed hundreds of people locally.

About £150 million was spent from the Stabilisation Fund to mitigate the effects of the GFC, including £44 million as part of a fiscal stimulus in 2009, under the banner that the expenditure would be 'temporary, timed and targeted'. Several of the assumptions made by policymakers about the effects of the fiscal stimulus on the Jersey economy were unclear and the reality was that this expenditure would do little to reduce unemployment in the banking industry (Corporate Services Scrutiny Panel, 2009, 2010).

Against this backdrop, medium term financial planning was finally introduced into Jersey to move away from short-term decision-making of yearly business plans. It was argued that this would provide flexibility, deliver efficiencies and encourage longer-term thinking whilst recognising that greater control should be exercised on government spending and imposing overall spending limits. Departments would be given funding certainty over a period of time and there would be an allocation of an annual central contingency fund accompanied by annual end-year flexibility for departments. The first Medium Term Financial Plan (MTFP) in 2012 was formulated at a time when Jersey was dealing with the fall-out from the GFC. The economic forecasts made during 2012 assumed a short recession and a return to trend growth by 2015. Whilst positive economic growth had returned by 2015, income tax receipts were £95 million lower in 2014 and 2015 than predicted at the time of MTFP (Corporate Services Scrutiny Panel, 2012).

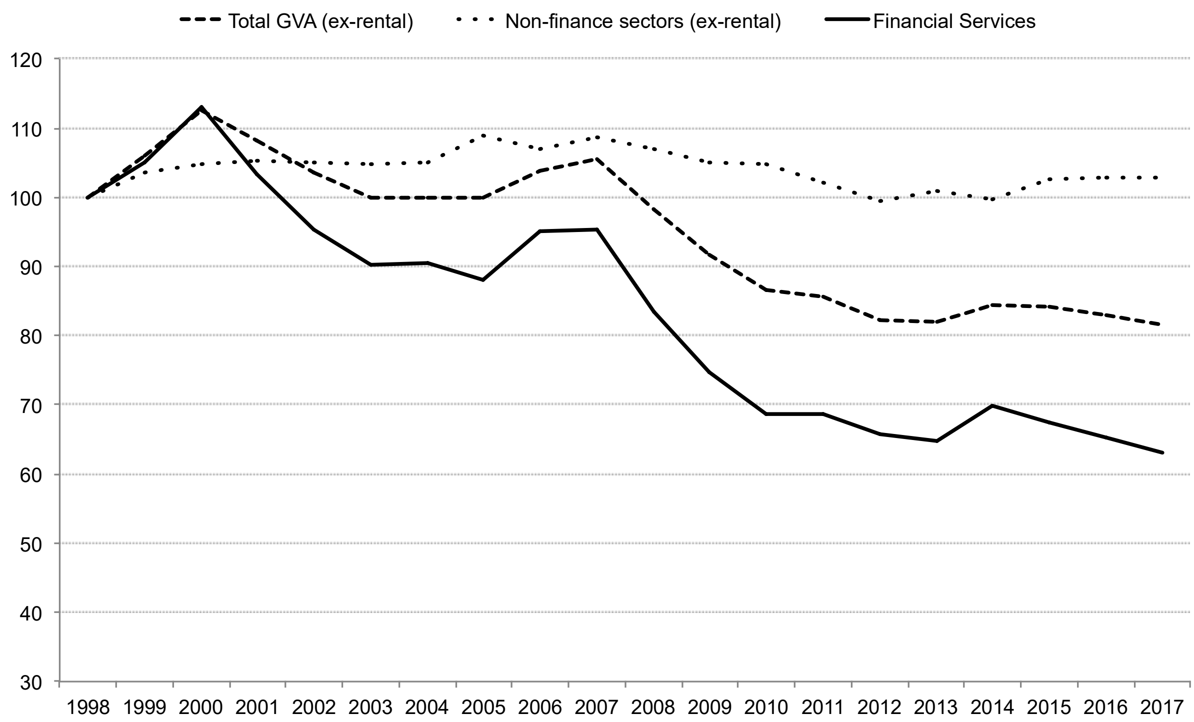
The challenges for Jersey's PROFIT economy and society

Jersey has long proven that a successful small island economy can enjoy a higher per capita GDP than larger states (Easterly and Kraay, 2000). However, since the early 2000s, there has been a significant decrease in living standards, caused by the contraction in financial services. Over the period 2000 to 2017, the GVA per head of population in Jersey decreased by almost a quarter (24 per cent) in real terms, with most of this long-term decline occurring after 2007: between 2007 and 2017 the GVA per head of population in Jersey decreased by almost a fifth (19 per cent). In 2017, Jersey's GDP per head of population was 24 per cent higher respectively than the UK's. However, if current trends continue, Jersey's GDP per head will be level with that in the UK by 2029 (Corporate Services Scrutiny Panel, 2017, p. 33).

Like many developed economies, Jersey has seen a trend of inferior value-processing-administrative functions being transferred to lower cost jurisdictions. The changes to the employment mix in Jersey can be illustrated by real-term changes in average earnings over the last thirty years. Between 1990 and 2001 there was real-term growth in earnings of 18 per cent and between 2001 and 2017, earnings remained flat in real terms, increasing only by 1.3 per cent over the period. After taking into account housing costs, median equivalised household income has decreased for those living in non-qualified (i.e. there is no automatic right to buy property) and social rental accommodation. Income inequality has increased, particularly after housing costs are included: twenty per cent of the working population are in relative low income. Income inequality was worse in Jersey in 2014/15 than in the UK (States of Jersey Statistics Unit, 2015). Whilst the benefits system pays for workers with five or more years residency, many local low paid workers are employed in agriculture and tourism and these workers often do not have five years' residency.

To sustain and increase *per capita* incomes requires that productivity growth be raised. Despite the economic growth plans of 2005 and 2012, the data shows limited evidence of any improvements (Figure 2). In the long run fundamental forces drive the growth of an economy: productivity; demographic changes and labour force participation. Jersey policymakers have long proclaimed that they understand the issues surrounding these forces but for various reasons have struggled to introduce policies to bolster productivity. Whilst the level of inward migration has been a growing concern to the electorate because of the pressure this puts on the island's infrastructure, this has been necessary to fill job vacancies in financial services, hospitality and agriculture businesses (the latter two sectors have traditionally relied on migrant workers, with their seasonal needs). Strong growth in net inward migration has placed additional demands on Jersey's infrastructure, particularly housing, and because of growing concerns about the future scale of migration, led in early 2019 to the establishment of a Policy Board to develop more responsive controls over who can come to live, work and access public services in Jersey. (Government of Jersey, 2019).

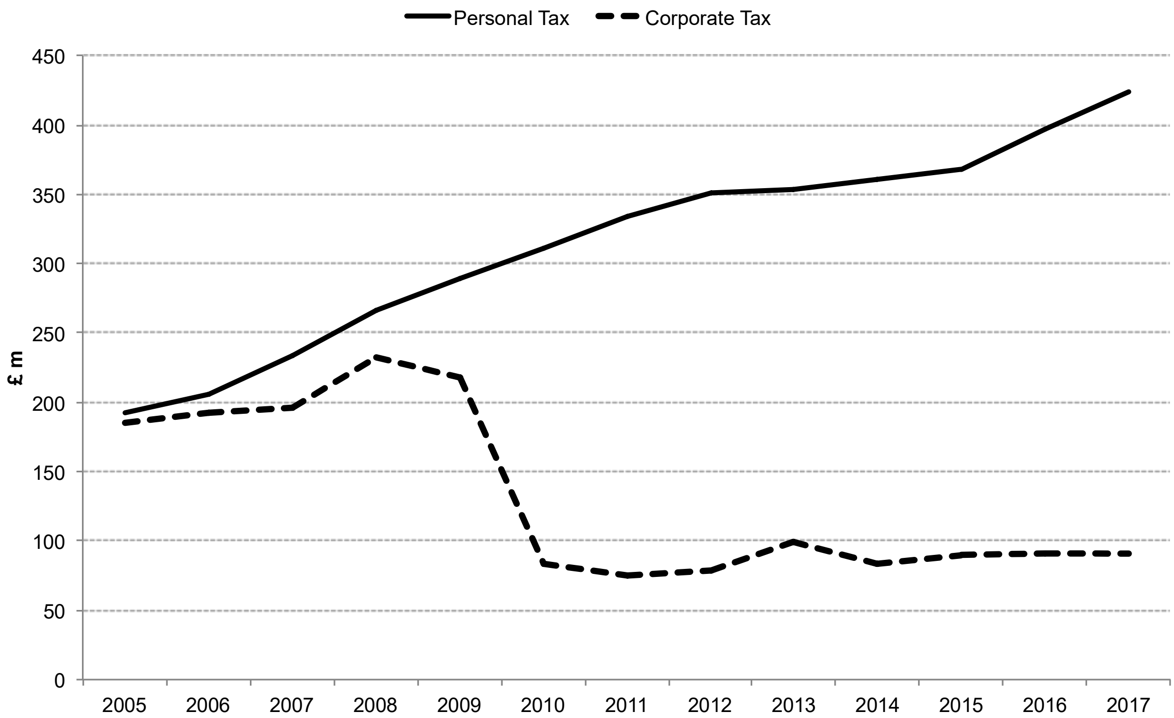
<u>Figure 2</u>: GVA per Full Time Employee: 1998-2017. (1998 = 100).



Source: Statistics Jersey

In essence, to remain economically prosperous, Jersey has required higher rates of growth in the financial services industry. However, the structural changes associated with the decline of the banking sub-sector has had a significant negative effect on income tax revenues (the highest earners were to be found in this sub-sector). Simultaneously, since the changes to the corporate tax system from the mid-2000s personal income tax has been required to contribute more to the island's revenues (see Figure 3).

Figure 3: Growth of personal tax and corporate tax receipts, 2005-2017.



Source: https://www.gov.je/Government/PlanningPerformance/BudgetAccounts/Pages/StatesofJerseyAccounts.aspx

A key challenge is political governance. As Le Herissier (1998) has argued, Jersey's system of government has exhibited four features: the conflation of legislative and executive powers in a single institution, the States Assembly; the high degree of internal autonomy secured by what is nominally a Crown dependency; the absence of political parties or permanent factions; and the tenacity of tradition (as witnessed by the strength of the Parish system). The States of Jersey, for reasons not altogether clear from history, developed a system whereby its various functions were delegated to Committees. The end result was a structure which would be familiar to those students of English local government when the committee system was in its heyday (Le Rendu, 2004, pp. 44-47). Over time, tensions arose with this system of government and it was replaced in 2005 by Ministerial government.

The introduction of political parties took until 2014, when a left-of-centre political party, Reform Jersey, fielded three candidates in the General Election. To this day, major difficulties are being experienced in developing a consensus which would result in significant democratic reform to the composition of the States Assembly (States of Jersey, 2019a). Ministerial government was accompanied by a more strategic approach and the partial introduction of managerialist thinking into the States of Jersey with its usual panoply of targets, business units and some outsourcing (States of Jersey, 2004). However, because the Jersey political culture is individualistic, and in the absence of party politics and the consensus which was found in the Committee system, frustrations have grown that the States Assembly needs democratic rejuvenation (States of Jersey, 2019b).

All politics in Jersey is very local and perhaps it is because of the strength of the Parish system that there has been widespread apathy in Jersey for political reform and party politics. A 2013 report showed that voter turnout in Jersey was lower than that recorded in all other OECD countries for which data is available (States of Jersey Statistics Unit, 2013). However, growing unease with some of the decisions made by the Council of Ministers and the States Assembly between 2014 and 2018 began to spill over into wider discontent with demonstrations against a site for the building of a new hospital and protests about using taxpayers' money for building an International Finance Centre (Jersey Evening Post, 2016; Bailiwick Express, 2016).

A witness statement by William Ogley, a former Chief Executive Officer to the States of Jersey, to the Independent Jersey Care Inquiry echoes some of the tensions documented by Le Herissier. After the 2005 changes, each senior civil servant (a Chief Officer) who headed a government department reported to the Chief Executive and to their respective Minister which, as Ogley (2016, p. 3) notes, led to a "significant lack of clarity in respect of supervision and accountability". A 2015 amendment to the Employment of States of Jersey Employees (Jersey) Law 2005 addressed this by making the Chief Executive Officer responsible for the administration and general management of the public service and in the implementation of corporate and strategic policies. This amendment was designed so that the expectations were that the Chief Executive Officer should lead the Chief Officers of Ministerial Departments in the administration and general management of the public service. However, grey areas remained, lines of accountability were unclear with many States Assembly members taking a different approach, and fundamentally, '[Government] departments were fiefdoms in law, with a siloed mentality, which meant that there was no shared ambition, no shared accountability, no collective responsibility and little cross-cutting activity' (Bailiwick Express, 2018a). There has been an absence of standardised expectations across the piece for governance; a lot of petty personal politics; and interference with the civil service which has led to a number of high profile resignations over the last decade. Historically, attempts to break the Lilliputian mindset by senior civil servants have either met with strong resistance or have resulted in the politicisation of the civil service.

The fragmented political process often influences the policymaking process in detrimental ways. Clark's (2013, p. 133) quip about policy-based evidence-making in "real life" islands is apt for Jersey. Evidence-based policymaking is often hard to come by with policy-based evidence making often at the fore. Examples would include the 2009 fiscal stimulus; the implementation of income support over the last decade; business grants and the 'back to work' programme. Each area would provide researchers with a rich research agenda.

For senior politicians who have not liked admitting mistakes and who have long enjoyed the "image/reality of internal stability, economic prosperity and political autonomy" (Mannin, 2006, p. 389), all of these challenges have threatened the rosy portrait to the outside world of a jurisdiction which is at ease with itself.

Conclusion

The drivers of economic success in larger countries – sound macroeconomic policies, strong institutions, effective governance, openness and a positive business environment – are not always found in small jurisdictions (IMF, 2013, IMF 2015). There has arisen a peculiar conjunction in Jersey, where a government, deeply rooted in tradition, came to preside over an extensively regulated and global industry in the form of financial services (Le Rendu, 2004; Le Herissier, 1974). Jersey has been particularly fortunate in that it has long enjoyed many of the characteristics associated with upper-middle and high-income countries, although over the last two decades, it has faced significant economic and social challenges. Whilst Baldacchino and Bertram's (2009) 'strategic flexibility' thesis is an attractive explanation for the development of Jersey's PROFIT economy over the last fifty years, it also has some shortcomings. The thesis has less to say about how an economy might slide down the 'development ladder' and as Clark (2013, p. 133) has noted, "even less to say about how 'strategic' decisions are made, who makes them, who benefits, and who is dispossessed in the process". For those who question the vulnerability thesis, Jersey provides a stark warning of how things can deteriorate through an incremental process, even in a successful economy, and how the economic resilience-building policies discussed by Briguglio et al. (2009) can be reversed. The proximate causes of Jersey's recent weaknesses, which threaten its position on the development ladder, might offer salient lessons for other PROFIT economies.

First, there is a danger of allowing a culture of complacency to develop. In Jersey's case, perhaps the 'capture of the state' thesis, discussed earlier in this article, might help to explain some of this complacency. In essence, since the 1970s, the government's primary focus has been on fulfilling the requirements of the finance sector at the expense of diversifying the economy, dealing with growing social problems, and addressing the failings in the public sector (Independent Jersey Care Inquiry, 2017a, p. 29). The success of financial services bred a belief that, because the world required offshore financial services, it also needed Jersey to deliver them. Until 2000, economic growth – driven by financial services – was assumed as a given and any check on this was regarded as temporary. Due to this mind-set, there has been a failure to understand that there have been structural changes to the economy over a much longer time scale, as illustrated by Figure 1, and policymakers have shied away from addressing the fundamental problems in Jersey which have been discussed in this article.

Secondly, and closely connected with complacency, is lethargy. Many problems can become too difficult and ignored. Twenty years ago, Jersey was described as a "town government writ large, with all its intimacies and inefficiencies" (Mitchell and Sikka, 1999, p. 40). The island has struggled to shake off this image and the rhetoric by senior politicians that Jersey is nimble and flexible has primarily only applied to adopting new financial services legislation (Hampton and Christensen, 2002). One of the most intractable problems discussed in this article is that of public sector reform and a new Chief Executive recruited from the United Kingdom was appointed in 2018 to enact significant changes, emboldened by new powers through changes in the Public Finance Law.

Thirdly, the culture of complacency and the lethargy is reflected in the social difficulty of implementing radical change. The island has become vulnerable in part because it has embedded power in a small number of groups and to accomplish change it would involve breaking these groups and social networks. In turn, this could cause politicians to accept social discomfort and upset, which they wish to avoid. The resistance to change was identified and discussed at length in the inquiry into historic child abuse in the island, and was referred to as 'The Jersey Way' (Independent Jersey Care Inquiry, 2017b, p. 63). Although a number of long-standing senior politicians did not contest their seats at the General Election in May 2018, the widespread dissatisfaction with the Council of Ministers did not lead to a political shift towards the left. Reform Jersey only gained an additional two seats, after contesting 19 out of 49 seats in the States Assembly. A new Chief Minister, Senator John le Fondré, formed a new Council of Ministers and included the chairman of Reform Jersey. Built around the mantra of "teams work, ego's don't", this is regarded as the most inclusive Council of Ministers to date (Bailiwick Express, 2018b; Jersey Evening Post, 2018a) and extensive changes have been promised for public administration in Jersey (Jersey Evening Post, 2018b; States of Jersey, 2018).

It is safe to say that economic and social stability in Jersey will be maintained while there is economic growth and the island can withstand economic downturns by drawing from its financial reserves. Economic growth currently depends on the ability of the island to survive the growing spotlight on its finance industry. The electorate has appeared willing to go along with policies which have supported the finance industry as it has delivered economic prosperity; but the ebbing away of finance and the need to pay for higher levels of public services and what that might mean for the future tax structure of the island, could lead to more public discontent. If public sector reform is perceived to be too radical for politicians and the general public and faster rates of economic growth from a reconfigured political and economic model are not delivered, then it is possible to envisage a scenario where Jersey's PROFIT economy becomes weakened and every danger that Jersey would fall down the rungs on the 'development ladder'.

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