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GPEG Commentary: Guernsey 2025 Budget & Emergency Mini-Budget

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GPEG PAPER

GUERNSEY 2025 BUDGET AND EMERGENCY MINI-BUDGET

Not one of us on the Island is happy that the Deputies have approved an unfunded budget for 2025.

Nor should the Fiscal Rules be broken (which were agreed in 2009 and updated in 2016). That red line shouldn't be crossed.

Without any income tax rise in 2025, the net deficit shown in the Budget becomes £49.8m. This is on top of the latest estimate of a deficit for 2024 of £62.7m.

With no tax rises in 2026 either, the net deficit can be expected to increase due to inflationary pressures, particularly with regard to health and education spending.

But then, according to the Deputies, all will be resolved in 2027 by introducing GST at 5%.

OR WILL IT?

Let's look at the deficit. It already includes the £30m benefit per year from 2025 for the anticipated introduction of a Pillar II corporate tax. The US election now puts this at risk. Biden supported Pillar II, but Trump and the Republicans are unlikely to adopt the legislation.

The deficit is also drawn after an optimistic credit for public sector pensions. It's in accordance with the latest actuarial valuation, but more prudent accounting would include an additional cost of around £20m for pensions.

That we have a financial crisis now seems widely accepted. So more taxation and cost cutting are the normal solutions but here it is seen by Mr Roffey and followers as an opportunity to increase the household incomes of a substantial proportion of the population. As a result, if we raise more GST to keep that proportion better off, we need to raise more money from taxes which means we need to raise more taxes…. you get the idea. As a very rough reckoner you need to raise 50% on top of the money required to fill the cash gap to keep the winners ahead on their living standards.

The actual extent of the money being raised to improve the living standards for part of the population is unclear. The final detail of the proposals is currently presumably being decided but the previous proposal was for a new 15% tax rate for earnings below £30,000 and also lower social security contributions, all at a time when we have a huge funding gap.

The amount proposed to be raised of £50m is unlikely to cover the 2027 deficit and certainly won't cover any of the annual capital expenditure of perhaps £100m each year. The level of planned States capital expenditure has moved erratically – because of the lack of funding.

Looking at paragraph 1.12 of the 2025 Budget, it states that one of the Fiscal Rules is: "a policy of long term balance". This would mean generating an ongoing revenue surplus that is sufficient to afford necessary capital and transformation projects."

For 2025, without an increase in income tax, we are looking at a deficit of £49.8m, together with pared back capital expenditure of £100m. That means generating more revenue of £150m in order to meet the Fiscal Rule in 2025.

We haven't been able to see or generate a proper calculation, but we conclude that it's more likely that a rate of GST of 10% will be necessary to cover the 2027 deficit plus capital expenditure. A rate of 5% is just dreamland.

We have to point out that the bases on which the financial accounts and budget are prepared are different, which makes it difficult to make comparisons or divisions. We are promised full consolidated accounts and compliance with IPSAS (International Public Sector Accounting Standards) for 2024. But the Budget for 2025 has not been prepared on this basis.

However, what we all should be looking at is cash. Having a Budget of revenue and costs is far from being the whole story. The Budget gives scant details of cashflow and nothing on the debt position. It would be a lot easier for everyone if the cash position was made clear. Instead, we are having to piece it together – and we arrive at important conclusions from doing so.

According to the Fiscal Rules, the States' total debt should not exceed 15% of GDP.

Looking at the 2023 Accounts (the latest detail available), we assess that debt at 31 December 2023 totalled £384m and comprised the Bond issue (£319m), the revolving credit facility (£30m) and depositors (£39m), less cash (£4m). GDP for 2023 was £3.48bn and 15% of that is £522m. That leaves borrowing headroom of £138m at the end of 2023 (£522m less £384m).

According to paragraph 4.14 of the 2025 Budget, the States has resolved that new debt of up to £200m could be used to fund the prioritised major capital expenditure portfolio this term. To accommodate the extra debt and comply with the Fiscal Rules, that would require GDP for 2025 to be £3.9bn, an implied GDP annual growth of 5.5%.

We note that these debt numbers are without including anything for Aurigny's long term leases, which accounting rules require to be recognised as debt.

If the starting point at the end of 2023 is debt of £384m, we estimate that funding is going to be required as follows:

Deficit for 2024 (less depreciation) (62.7 – 29.6)	£33.1m
Capital expenditure for 2024 (estimated)	£150m
Deficit for 2025 (less depreciation) (49.8 – 30.2)	£19.6m
Capital expenditure for 2025 (per Budget)	£100m
Deficit for 2026 (less depreciation) (assume as for 2025)	£19.6m
Capital expenditure for 2026 (assume as for 2025)	£100m
Total	£422.3m

Note: we adjust for depreciation as being the only assumed non-cash item.

The proposal in the 2025 Budget of new debt of £200m leaves a substantial amount of £222.3m unfunded. And this is before reaching the nirvana of GST in 2027.

This is why P&R are urgently talking about cancelling capital projects. We will only be able to afford absolutely essential capital spending. And these numbers show that's until at least 2027.

We refer to GPEG's paper published in January 2021 titled Capital Expenditure in Guernsey, which set out the need to categorise and prioritise capital expenditure. The warnings have been there - and the pressure is mounting.

The States are continuing to add to the funding burden that the new Deputies will inherit after the 2025 election. The new Deputies will be met with a crisis that won't be solved by the GST-plus plan to introduce GST at 5%. They won't have much time to get to grips with the funding position, let alone find solutions.

It is hard not to conclude that the red line on meeting the Fiscal Rule on debt will be crossed before we get to GST. Something will have to give: rip up the Fiscal Rules or cut expenditure or sell more investments.