Report of the Inflation Strategy Group

January 2020

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Government of JERSEY

Foreword by the Deputy Chief Minister

Jersey enjoys a high standard of living compared to many other countries, with low levels of unemployment and high average earnings. However, the Government cannot be complacent as these significant advantages can be quickly eroded if the cost of living in the Island, and the cost of doing business, rises more quickly than incomes.

The last ten years have seen significant challenges in this respect, with earnings growing no faster than inflation since 2008. Much of this was due to the unprecedented challenges presented by the global financial crisis and the prolonged economic downturn that followed. Recent years have been more encouraging but the significant spikes in inflation in 2017 and 2018 have again put pressure on living standards.

While the Inflation Strategy Group was formed in response to a large temporary increase in inflation, it is not a short-term issue that can be easily fixed and forgotten about. Government must remain vigilant at all times to ensure that inflation can be kept relatively low and predictable. We will not be able to mitigate all cost pressures, especially where these come from increases in global commodity prices or exchange rate fluctuations, but ministerial colleagues and I have considered a number of practical approaches so that government sets the right conditions to support low and stable inflation over the long term.

Government cannot do this alone. It is important that businesses do their bit to contribute to price stability. There is also a key role for the Jersey Consumer Council, who will be supporting Ministers in delivering this Strategy.

I want to thank the Chief Minister, the Minister for Treasury and Resources, and the Minister for Education for their support and their valuable contributions to the Inflation Strategy Group. This report sets out our initial findings and actions, and we will continue to monitor progress and remain alert to any future developments in inflation.

Inflation is more than just a dry, technical measure. It affects the lives and living standards of all Islanders, and particularly those who are less well off. Achieving low and stable inflation is key to achieving a number of the strategic priorities of this Council of Ministers, including creating a sustainable, vibrant economy and improving the standard of living. Jersey needs to remain competitive to achieve our aim to create a sustainable, vibrant economy. In addition, keeping the Island affordable for all residents[1] is central to our aim to reduce income inequality and improve the standard of living.

Senator Lyndon Farnham
Chair of the Inflation Strategy Group
Deputy Chief Minister
Minister for Economic Development, Tourism, Sport and Culture

[1] Affordable living is about being able to afford what you need to lead a healthy, happy and productive life.

Executive Summary

Jersey had four years of historically low inflation from 2013 to 2016. However, inflation started to pick up in early 2017 due to rising global oil prices and the significant depreciation of sterling following the UK's 2016 referendum on membership of the EU. Inflation continued to increase, and RPIX inflation (which excludes mortgage interest payments) peaked at 4.2% in the middle of 2018. The biggest driver of inflation in recent years has been housing costs, though there were also significant contributions from household services, leisure services and motoring.

Monetary policy is the preferred policy instrument to control inflation but as Jersey is in a currency union with the UK, monetary policy is set by the Bank of England to meet the inflation target for the UK of 2% CPI inflation. This means that the interest rates set by the Bank of England at any one time may not always be completely appropriate to manage demand and control inflation in Jersey.

However, the Government of Jersey has other policy levers that can directly affect and influence prices across the economy, and hence the rate of inflation, for example:

- Indirect taxes, e.g. impôts and GST
- Prices/fees charged by government or by States-owned entities
- Competition and productivity

Government's overall priority is to improve income equality and the standard of living - aiming for low and stable inflation is only one part of how we will meet the overall priority. A number of actions have been developed, to set out how Government will pursue low and stable inflation.

Action 1

The Government will consider the impact on inflation of any changes to indirect taxes, including the production of an assessment of the impact on inflation of changes to duties. This will inform broader policy objectives, for example to achieve a reduction in the use of carbon-based fuels, tobacco or alcohol.

Action 2

The Government will seek to keep its own price increases low, while ensuring sufficient revenue to make the investment necessary to maintain services. Increases in government charges and fees will aim to average less than 2.5% per year in the long run (i.e. over a ten-year period). This will help to ensure that the Government contributes to low and stable inflation with a long-run average of 2.5%.

In the case of user-pays charges, the principle is that the cost of providing these services is fully reflected in the price, therefore there may be justification for increasing or decreasing prices in line with costs – otherwise non-users may end up subsidising users if the shortfall is funded by general taxation. While efficiencies should still be sought before passing on any price increase, the general principle remains that prices should reflect the cost of providing the service.

Action 3

The Government will develop and publish a fees and charges policy. This will facilitate each department to consider the overall impact on inflation of the aggregate changes to fees and charges within their control each year.

Action 4

Should any significant new charges be planned, the Government will consider the impact of this on inflation and living costs and include this analysis to support decision-making. The Minister will bring a change to Standing Orders so that all relevant Propositions presented to the Assembly will include a brief 'inflation impact assessment'.

Action 5

The Government will consider the impact on inflation from any price rises over which they have influence or control (including States wholly-owned entities, social housing providers and fee-paying schools) and be mindful that any price increases above 2.5% will put upward pressure on the trend rate of inflation. However, any price changes should be set with regard to the specific circumstances of the sector concerned, in order to protect consumers while ensuring sufficient revenues to support continuation of vital services and to enable the necessary investment.

As with Government charges, wholly or majority States-owned entities should consider the impact any change to their prices might have on the trend rate of inflation, whether the price increase is above 2.5% or not. Where the potential impact on the overall inflation rate is significant, States-wholly-owned entities should consult, subject to regulatory best practice, with the Government before implementing price increases. States-majority-owned entities are encouraged to consider the impact on inflation of price increases and are encouraged to seek an inflationary impact assessment from Statistics Jersey as part of their consideration.

Action 6

The Government will ensure continued support for the JCRA and will review and assess the competition framework to ensure that it remains fit-for-purpose. The Government will work with the JCRA to ensure competition policy is directed at those sectors with potentially significant impacts on the living standards of households and the competitiveness of businesses.[2]

The Government will improve consumer knowledge by providing enhanced support to the Jersey Consumer Council to invest in existing price comparison resources and developing new comparisons across a range of different markets, starting with Grocery Watch.

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[2] These would relate to essential services such as utilities and transport as well as accommodation and food.

Contents

1. About the Inflation Strategy Group

The last anti-inflation strategy for Jersey was produced in 2008. In the period since then the Island experienced four years of historically low inflation from 2013 to 2016, and in 2017 inflation started to rise.

Senator Lyndon Farnham, the Deputy Chief Minister and Minister for Economic Development, Tourism, Sport and Culture, formed the Inflation Strategy Group in February 2019 to consider what the Government could do to maintain low and stable inflation in Jersey. The membership is:

- Inflation Strategy Group Chair, Senator Lyndon Farnham
- Chief Minister, Senator John Le Fondré
- Minister for Treasury and Resources, Deputy Susie Pinel
- Minister for Education, Senator Tracey Vallois

The Group has been supported by the Chief Economic Adviser and other officers with the relevant expertise. Its objective was to consider and develop policies that would support low and stable inflation, to produce a new strategy document and monitor the implementation.

The Inflation Strategy Group remains in place and will periodically review the progress of the strategy, particularly in response to any changes in Jersey's economic circumstances.

2. Background to inflation

The Retail Prices Index (RPI) is the official measure of prices and inflation in Jersey. Statistics Jersey produces the RPI, based on prices collected on or around the 15th day of March, June, September and December each year.

> *"Conceptually, the RPI may be thought of as a 'shopping basket' which contains the various goods (e.g. bread, televisions, wardrobes) and services (e.g. doctors, dentists, hairdressers) purchased by resident households in Jersey. As the prices of the various items in the basket change over time, so does the total cost of the basket."*
>
> Source: Statistics Jersey

The change in prices of the items in the basket from one quarter to the next is used to construct an overall index that enables price comparison over time. For example, the index can be compared to the same month of the previous year, to get the *annual inflation rate*. Statistics Jersey then uses similar measures from the UK and Guernsey to compare movements in the price level in Jersey with nearby comparators.

> *"The Jersey RPI is calculated from over 5,000 separate price quotations in total. The same basic approach is adopted in other jurisdictions (e.g. in the UK by the Office for National Statistics, ONS) for the compilation of consumer price indices. Structurally the RPI is composed of 14 groups; each group is composed of several sections (there are 85 sections in total); and each section is made up of a number of representative items."*
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> Source: Statistics Jersey

Statistics Jersey produces quarterly reports that set out the rate of price increase (i.e. inflation) compared to the same month a year previous, and compared to the previous quarter. This is presented both on an overall basis (i.e. the whole 'basket' of goods) and by group (i.e. broad categories of spending):

Food	Tobacco	Household goods	Personal goods and services	Leisure goods
Catering	Housing	Household services	Motoring	Leisure services
Alcoholic Drink	Fuel and Light	Clothing	Fares and travel	

Statistics Jersey also produces statistics for the price index and inflation rate of a number of variations to the main 'basket':

- RPI(X) - excludes mortgage interest payments
- RPI(Y) - excludes mortgage interest payments and indirect taxes eg. GST and duties
- RPI Low Income - for households in the lowest 20% of household incomes
- RPI Pensioners – for pensioner households

While an *increase in prices* is referred to as inflation, it is important to distinguish this from an *increase in inflation*, which is an acceleration of price increases. Similarly, a *fall in prices* is referred to as deflation but a *fall in inflation* may not necessarily mean reductions in the price level – just a deceleration to a lower (possibly still positive) rate of growth in prices.

In this report, Jersey's inflation rate has been compared to the UK's. This is the most appropriate comparator as Jersey shares a currency with the UK and monetary policy is set for both jurisdictions by the Bank of England. As the UK is Jersey's biggest trading partner, the vast majority of our imports either come from the UK or transit through the UK from external markets.

The weighting of items within the respective baskets in the UK and Jersey reflect expenditure patterns in each jurisdiction. For example, differences in the heating fuel market means that the weighting of *gas* is much higher in the UK while the weight of *oil and other fuels* is higher in Jersey. Household services have a much higher weight in Jersey than the UK, and this is driven primarily by the weight of *school fees* in Jersey – which is ten times the weight in the UK. However, the similarities are greater than the differences, with most groups having a very similar weight in each jurisdiction. Figure 1 compares the weighting of the RPI groups in each jurisdiction.

Figure 1 - Comparison of UK and Jersey RPI Group weights

Group	Jersey weight	UK weight
Food	11%	10%
Catering	5%	5%
Alcoholic drink	5%	6%
Tobacco	2%	2%
Housing	20%	26%
Fuel and light	4%	4%
Household goods	6%	7%
Household services	13%	6%
Clothing and footwear	3%	4%
Personal goods and services	7%	4%
Motoring	10%	12%
Fares and other travel	3%	3%
Leisure goods	3%	3%
Leisure services	11%	10%

The headline measure of inflation in the UK is based on the Consumer Prices Index including housing costs (CPIH). This is broadly similar to Jersey's RPI measure, though it differs in a number of ways[3]. While it is possible to remove these differences by calculating a directly comparable figure from published UK data, this is not available on a group-by-group basis. Therefore, for the purpose of the analysis to inform this report, Jersey's RPI has been compared to CPIH in the UK (as both include owner-occupiers' housing costs) whereas

[3] There are some items that are included in the CPIH basket that are not in the RPI basket and vice versa, plus the RPI and CPIH use alternative approaches to calculate certain items relating to housing costs.

RPIX in Jersey has been compared to CPI in the UK (both exclude owner-occupiers' housing costs).

The costs of high inflation

There are several ways in which high inflation is likely to be harmful:

1. Negative real interest rates (where the rate of inflation is higher than the interest rate) can be damaging to those with significant savings or relatively fixed incomes, for example retired people.
2. High inflation can affect competitiveness, if a business's costs are increasing faster than costs for competitor firms located in other jurisdictions.
3. It can be difficult for firms and households to plan, as costs can change rapidly in a short time period.
4. There are potentially significant administrative costs with businesses frequently changing prices.

There is a significant body of research into what level of inflation is harmful to economic growth, with a wide range of estimates for the threshold. For example, research by the International Monetary Fund (IMF) suggests that annual rates of inflation above 1-3% may slow growth in advanced economies, while the threshold is 11-12% for developing economies[4]. Evidence from the United States suggests a quarterly threshold of between 0% and 1.5%, above which inflation has a significant negative effect on growth[5].

Deflation (i.e. falling prices) can also be damaging to the economy. In particular, if there is an expectation of prices falling it may cause households to delay purchases in order to benefit from getting these goods and services cheaper in the future. This can act as a drag on demand, slowing economic growth and potentially causing further deflation. If wages fail to adjust, this can lead to job losses and a further drag on demand – resulting in further deflationary pressures.

Differential impacts of inflation

Different households may feel the impact of a certain period of high inflation or deflation differently. For example, if the cost of heating oil rises, this will primarily affect those with oil-fired heating systems. However, if the cost of food rises this is likely to affect all households – but will be felt more acutely by households on low incomes, as they tend to spend a greater proportion of their income on food.

One example of where this differential impact can clearly be seen in Jersey is when there are changes to interest rates on mortgages. For example, Figure 2 shows that the significant falls in the Bank of England's Bank Rate in 2008 and 2009 caused inflation to turn negative (representing deflation) but this was not experienced by pensioner households (on average), as they are less likely to have mortgages.

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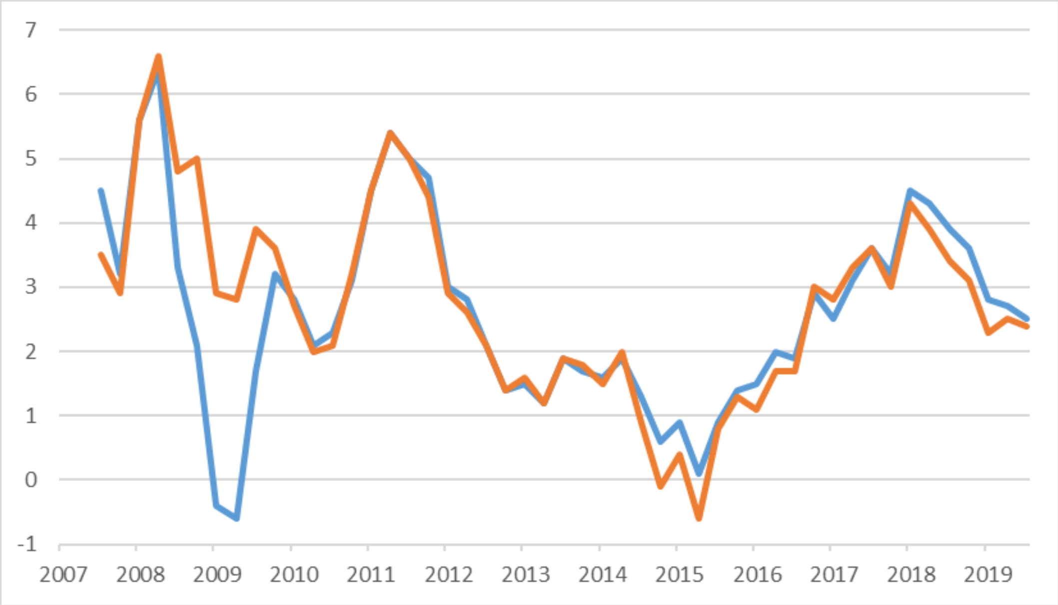
[4] https://www.imf.org/external/pubs/ft/wp/2000/wp00110.pdf
[5] https://www.researchgate.net/publication/311413446_Inflation_and_Growth_An_Estimate_of_the_Threshold_Level_of_Inflation_in_the_US

Figure 2 – RPI inflation (blue line) compared to RPI pensioner inflation (orange line)



Source: Statistics Jersey

Inflationary pressure

There are broadly two types of inflation, depending on the cause:

1. Demand-pull inflation occurs where demand in the economy increases faster than supply, bidding up prices. This may occur for example if there is an increase in the government deficit, adding to demand.

2. Cost-push inflation occurs when there is a reduction in supply due to an increase in the cost of producing goods and services, for example an increase in global oil prices.

The interaction of cost-push and demand-pull inflation may contribute to inflationary pressure, or a 'wage-price spiral'. For example, if a price shock results in a contraction in supply and an increase in inflation, this may result in increased wage pressures that in turn could stoke demand and cause further upward pressure on prices.

3. Inflation trends in Jersey

Jersey had four years of historically low inflation from 2013 to 2016. However, inflation started to pick up from early 2017. This was partly due to increasing global oil prices (from $30/barrel in January 2016 to $80/barrel in October 2018) but was primarily related to the 15% depreciation of sterling following the UK's 2016 referendum on membership of the EU. The depreciation of sterling resulted in an increase in the cost of imports, which fed into increased consumer prices. Both Jersey and the UK saw a spike in inflation. Figure 3 demonstrates that, on a trade-weighted basis, there has been no sustained recovery in sterling since the referendum.

Figure 3 - Sterling broad effective exchange rate index (Jan 2005 = 100)

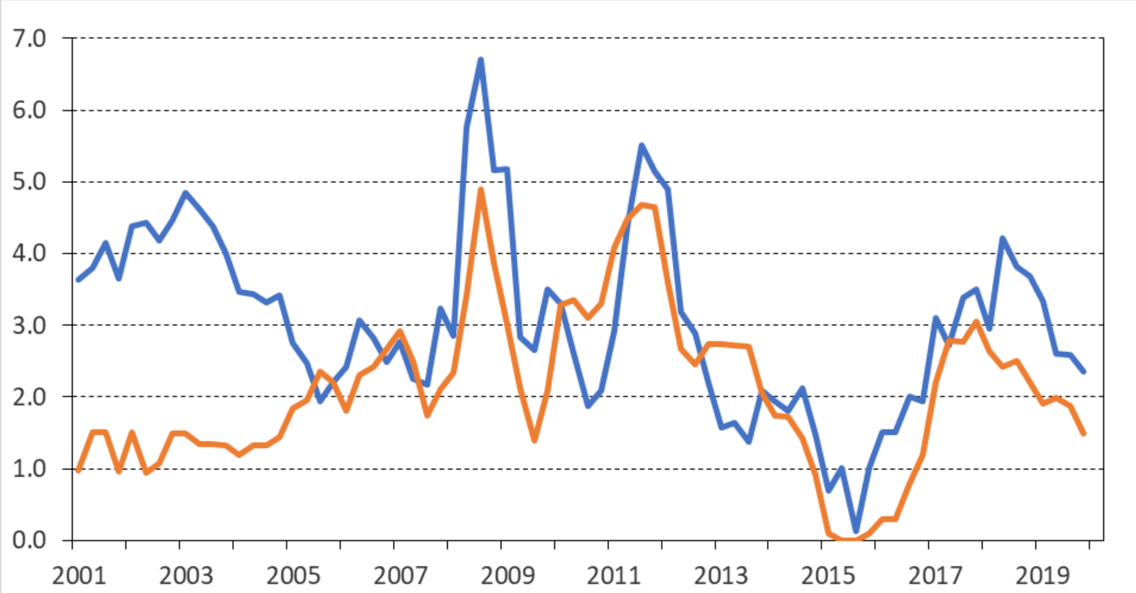
Source: Bank of England, data to 30 January 2020

The sterling exchange rate weakened significantly from May to October 2019, as the likelihood of a no-deal Brexit appeared to strengthen, though this has been reversed since mid-October with the partial resolution of an eventual Brexit withdrawal. Neither the Bank of England's 'conditioning assumption' in their recent Monetary Policy Report[6] nor the median of independent forecasts collected by the UK Treasury[7] anticipate any further significant improvement in the sterling exchange rate in 2020, and there remains the potential for further falls should developments lead to a more pessimistic outlook for ongoing UK-EU trade relations.

Figure 4 shows that the inflation rate in Jersey began to increase further and diverge from that in the UK in the middle of 2018, when Jersey's RPIX inflation hit 4.2%, with prices in Jersey rising at almost twice the rate in the UK (as measured by the CPI). While inflation has eased off since that peak, it remains above the ten-year average (2.6%), and above the UK's rate, which has also fallen.

6 https://www.bankofengland.co.uk/monetary-policy-summary-and-minutes/2020/january-2020
7 https://www.gov.uk/government/statistics/forecasts-for-the-uk-economy-january-2020

Figure 4 - Jersey RPIX inflation (blue line) and UK CPI inflation (orange line) (% annual change)



Source: Jersey RPIX = RPI excluding the cost of mortgage interest payments (Statistics Jersey)
UK CPI = Consumer Prices Index, excluding owner occupiers' housing costs (Office for National Statistics)

Figure 5 shows the contribution of each group (i.e. category of spending) to the overall growth in Jersey's RPI over the two years from December 2017 to December 2019. The biggest driver of inflation has been housing costs – including rent and mortgage interest payments. Some of this was related to rising mortgage rates resulting from the ¼% increase in the Bank of England Bank Rate in August 2018 with much of the remainder related to significant increases in the cost of residential property in Jersey.

Figure 5 - Contribution of groups to overall inflation December 2017 to December 2019

Group	Percentage point contribution
Housing	1.8%
Household services	1.3%
Leisure services	0.9%
Motoring	0.6%
Alcoholic Drink	0.4%
Food	0.4%
Fuel and Light	0.3%
Catering	0.3%
Tobacco	0.2%
Personal goods and services	0.1%
Leisure goods	0.1%
Household goods	0.1%
Fares and travel	0.0%
Clothing	-0.1%
Overall	**6.5%**

Source: Statistics Jersey; Economics Unit calculations

However, as Figure 5 shows, there were also significant contributions from household services (which includes postage, telecoms, domestic services and school fees), leisure services (holidays, TV licences, entertainment, and recreation activities) and motoring (purchase of motor vehicles, motor fuels, insurance, and other related costs). Clothing was the only group to make a negative contribution to inflation over this period.

Inflation Strategy Group

In response to the high levels of inflation seen in recent years and concern about the impact on living standards, the Inflation Strategy Group was formed to assess potential policies that might be introduced to support low and stable inflation in Jersey. This is led by the Deputy Chief Minister and Minister for Economic Development, Senator Lyndon Farnham; joined by the Chief Minister, Senator John Le Fondré; the Minister for Treasury and Resources, Deputy Susie Pinel; and the Minister for Education, Senator Tracey Vallois. The group is supported by the Chief Economic Adviser and the Chief Statistician.

The objective of the group is to produce a new strategy and policy on inflation, and monitor its implementation.

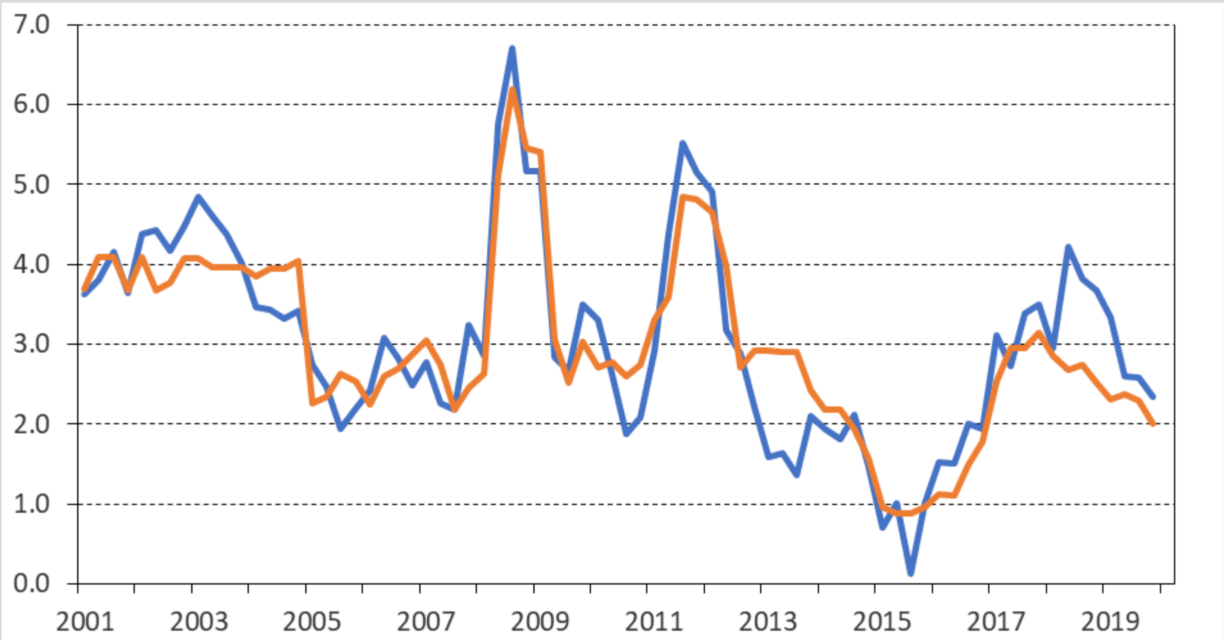
Longer-term trend in inflation

The Fiscal Policy Panel (FPP) has undertaken analysis and modelling to consider Jersey's 'trend rate' of inflation that would be expected over the long run given inflation in the UK. After controlling for changes in Jersey's Goods and Services Tax (GST) and the UK's Value Added Tax (VAT), for crude oil prices and for the introduction of the Competition Law in Jersey, the FPP concluded:

> *"while these two measures of inflation may diverge at times, on average and most of the time changes in Jersey RPIX are similar to changes in UK CPI with Jersey inflation tending to be a little higher."*
>
> Source: Fiscal Policy Panel, Advice for Government Plan 2020-23

Figure 6 shows that the model provides a reasonably good fit to past changes in RPIX, but there are a few outliers. In particular, Jersey inflation was lower than the model can explain in 2012/13 and higher in 2018/19.

Figure 6 – Inflation model – actual (blue line) vs fitted (orange line)



Source: Jersey RPIX = Jersey RPIX inflation from Statistics Jersey
RPIX model = fitted line using inflation model

Notwithstanding these divergences, the model appears to perform well in explaining the relationship between the two inflation rates in the long run. Therefore, on the assumption the UK's CPI inflation is close to its 2% target on average[8], the FPP estimated that Jersey's RPIX inflation is expected to average around 2.5% in the long run, with RPI inflation a little higher at 2.6%.

[8] Monetary policy in the UK has been independent since 1997. CPI inflation has averaged 2.0% from 1998 to Q4 2019.

4. Key levers to influence inflation

Monetary policy is the preferred policy instrument to control inflation but as Jersey is in a currency union with the UK, monetary policy is set by the Bank of England to meet the inflation target for the UK of 2% CPI inflation. This means that the interest rates set by the Bank of England at any one time may not always be completely appropriate to manage demand and control inflation in Jersey.

However, the Government of Jersey has other policy levers that can directly affect and influence prices across the economy, and hence the rate of inflation:

First, the Government sets the rates of duties/impôts that affect the price of alcohol and fuel for example. It can also change other indirect taxes i.e. taxes on purchasing goods and services, such as GST. Although these taxes could be absorbed by the seller, typically higher duties are at least partly passed on to the consumer in the form of higher prices.

Second, the Government has control or influence over a number of prices/fees in Jersey. For example:

- Government charges fees for a number of services and therefore sets prices.
- As a shareholder in a number of public corporations, Government can play a role in determining the price of key goods and services along with social housing rents.
- Government is responsible for approving fee increases in the States-owned fee-paying schools and influences fees charged at a number of private fee-paying schools through subsidies. Similarly, government subsidises some private healthcare costs (particularly GP visits) and therefore affects the post-subsidy price.
- Government directly sets prices for some sectors, e.g. public rank taxis.

Third, the Government has a responsibility to ensure effective competition in the pricing and provision of goods and services in the private sector. Uncompetitive markets, through monopoly and cartels for example, not only lead to higher prices for consumers but there is also evidence that they may promote higher inflation rates. Similarly, improvements to productivity in the market sector can help to reduce prices and increase wages, thereby improving affordability and the standard of living.

5. What Government will do

Inflation is a cross-cutting issue and there are many government policy areas that can impact on inflation and on the cost of living generally. The Housing Policy Development Board is developing proposals to improve supply and affordability of housing and any reduction in house prices will result in a reduction to the rate of inflation.

There are also areas where government will have an impact on the cost of living but not necessarily on the rate of inflation. For example, the increase to fuel duties in response to the declaration of a climate emergency will result in an increase to measured inflation. However, the funds raised from this will be used to support new policies in a range of areas, including transport and energy. Depending on how this is spent, it may impact on inflation (for example if bus fares are reduced) or it may impact on the standard of living for some households without reducing measured RPI (for example if it is used for a scrappage scheme for inefficient boilers or motor vehicles).

Government's overall priority is therefore to improve income inequality and the standard of living - aiming for low and stable inflation is only one part of how we will meet the overall priority. A number of actions have been developed, to set out how Government will seek to support the aim of low and stable inflation.

The actions are broken down into four categories:

1. Indirect taxes

The largest single element of indirect taxes in Jersey is collected through GST (£93m in 2018 including International Service Entity fees, compared with a total for all duties of £62m). Any future increase in GST would be highly likely to be at least partly passed on in prices and would therefore result in an increase in inflation. However, one-off increases in GST do not have a permanent effect on inflation and tend to reduce total demand and hence general price pressures. Therefore, it is not recommended that any changes be made to the GST rate in order to influence inflation but rather that GST policy is set in line with Jersey's tax policy principles.

The next largest element of indirect tax is from excise duties / impôts. These are levied on alcohol, tobacco, fuel and importation of motor vehicles – all goods that have negative *externalities*, i.e. additional costs associated with their consumption that are not included in the basic price paid by the consumer. Therefore, it is appropriate to charge additional duties in order to reflect some of the cost to society.

Action 1: The Government will consider the impact on inflation of any changes to indirect taxes, including the production of an assessment of the impact on inflation of changes to duties. This will inform broader policy objectives, for example to achieve a reduction in the use of carbon-based fuels, tobacco or alcohol.

2. Prices under the influence of government

The goods and services supplied by Jersey's government, public corporations and schools make up a significant proportion of the overall inflation basket. Therefore, the prices charged for these goods and services contribute directly to inflation. As indicated in section 3, the FPP has estimated that Jersey's RPIX inflation is expected to average around 2.5% in the long run. Therefore, any price increase above 2.5% will make it more likely that Jersey's inflation rate will 'overshoot' its trend rate.

Price increases for goods and services provided by the public sector should be kept as low as possible, and efficiencies should be sought before passing on any increase in costs. However, it is accepted that some cost increases will need to be passed on and Government should not seek to undermine the viability of providing these key services. Therefore, there may be some exceptions where larger increases are permitted as a one-off or for a period, to ensure that sufficient resources are available to invest in ongoing provision of services.

Action 2: The Government will seek to keep its own price increases low, while ensuring sufficient revenue to make the investment necessary to maintain services. Increases in government charges and fees will aim to average less than 2.5% per year in the long run (i.e. over a ten-year period). This will help to ensure that the Government contributes to low and stable inflation with a long-run average of 2.5%.

In the case of user-pays charges, the principle is that the cost of providing these services is fully reflected in the price, therefore there may be justification for increasing or decreasing prices in line with costs – otherwise non-users may end up subsidising users if the shortfall is funded by general taxation. While efficiencies should still be sought before passing on any price increase, the general principle remains that prices should reflect the cost of providing the service.

The new Public Finances Manual[9] includes a requirement that Departments get approval from the Treasury Minister for any annual increase in prices of more than 2.5%. When considering whether to grant approval, the Treasury Minister will seek to establish the impact this might have on the overall rate of inflation. While Departments will continue to have delegated authority to increase prices by 2.5% or less, the responsibility will be on the Department to consider the impact this might have on the overall rate of inflation and consult with the Treasury Minister if the impact is expected to be significant.

A more coordinated approach needs to be taken to considering the overall level of fees and charges levied by the Government. Any new charges should be subject to scrutiny to determine the impact they will have on inflation.

Action 3: The Government will develop and publish a fees and charges policy. This will facilitate each department to consider the overall impact on inflation of the aggregate changes to fees and charges within their control each year.

[9] https://www.gov.je/Government/PlanningPerformance/PublicFinances/Pages/PublicFinanceManual.aspx

Action 4: Should any significant new charges be planned, the Government will consider the impact of this on inflation and living costs and include this analysis to support decision-making. It is envisaged that all relevant Propositions presented to the Assembly will include a brief ‘inflation impact assessment’.

In addition, the Government and the Jersey Competition and Regulatory Authority (JCRA) can have considerable influence over the prices charged by public utilities, including electricity, water, post, harbours and airport, and telecoms; and by social housing providers. A number of these require significant capital investment, in order to maintain services, and therefore their cost base may not necessarily grow in line with the overall inflation rate in Jersey. However, as pricing in these sectors has a potentially significant impact on inflation, Government as shareholder and the JCRA as regulator should seek to ensure that any proposed price rises are necessary and justified, particularly if they are likely to exceed a long-term average of 2.5% annually.

There are specific arrangements in place for prices in some areas, for example:

- Social housing rent increases have been capped since 2019, such that prices will rise by RPI+0.75% each year but only within a range of 2.5% to 4.0%. This will allow continued investment in social housing but the cap will prevent rent rises from prolonging inflationary pressures when the general price level (i.e. RPI inflation) has been increasing faster than 3.25% in the previous year.
- Public rank taxi fares are set by the Infrastructure Minister each year, in line with the change in the costs faced by taxi drivers – as calculated by Statistics Jersey.
- Prices in the telecoms market, for Jersey Post and for the Ports of Jersey are regulated by the JCRA.

As these individual approaches reflect the specific circumstances in each of these sectors, the Inflation Strategy Group is not proposing any significant change to the existing arrangements.

Action 5: The Government will consider the impact on inflation from any price rises over which they have influence or control (including States wholly-owned entities, social housing providers and fee-paying schools) and be mindful that any price increases above 2.5% will put upward pressure on the trend rate of inflation. However, any price changes should be set with regard to the specific circumstances of the sector concerned, in order to protect consumers while ensuring sufficient revenues to support continuation of vital services and to enable the necessary investment.

As with Government charges, wholly or majority States-owned entities should consider the impact any change to their prices might have on the trend rate of inflation, whether the price increase is above 2.5% or not. Where the potential impact on the overall inflation rate is significant, States-wholly-owned entities should consult, subject to regulatory best practice, with the Government before implementing price increases. States majority-owned entities are requested to consider the impact on inflation of price increases and are encouraged to seek an inflationary impact advice from Statistics Jersey as part of their consideration.

3. Fiscal policy

While monetary policy is the optimal policy instrument with which to influence inflation, there is a role for fiscal policy. Government is a significant purchaser in Jersey's economy, but also affects demand from the private sector through taxation and payments that affect household income. This means that there is the potential for fiscal policy to exacerbate the economic cycle by adding further to demand when the economy is booming, and therefore exacerbating any demand-led inflation. Running budget surpluses when the economy is above trend should help to dampen the cycle and therefore avoid making any inflationary pressures worse.

The Government of Jersey will therefore aim for fiscal policy to be counter-cyclical, following the advice of the Fiscal Policy Panel.

4. Competition and productivity

If a market were 'perfectly competitive', no single firm would have the ability to set prices – each seller would have to accept the price decided by the market as charging a higher price would result in a complete loss of market share to competitors. In the opposite situation, with a monopoly, there is only one seller who therefore has significant power to set prices at the level that is most beneficial to them – generally much higher than the price that would be set in a competitive market.

In between the extremes of perfect competition and monopoly, therefore, any move to more competition will, all else equal, give firms less pricing power and therefore reduce prices. As a small economy, Jersey faces particular challenges in ensuring sufficient competition.

> *"In small-island economies, such as Jersey, it is just as important that markets work well as it is in larger economies. But in smaller jurisdictions competition policy, and regulation where competition is not possible, faces particular challenges. First, in some markets not exposed to international competition, there is not as much scope as in larger economies for there to be effective competition. Second, there are economies of scale in regulation and competition policy itself, so their cost per resident is greater than in large economies. This underlines the importance of the institutions that carry out competition and regulatory policy working as effectively as possible."*
>
> Source: Sir John Vickers, foreword to Oxera review of the Jersey regulatory and competition framework

There is a trade-off in that a small domestic market means there is a limit to the number of market competitors that can operate at an efficient scale. The Oxera review of Jersey's regulatory and competition framework[10] set out a number of repercussions from this and emphasised the need for a *culture of competition* to enable competition law to work effectively. Oxera advised that this places particular importance on activities designed to promote a competitive environment and raise awareness of competition policy and its benefits among businesses, consumers and public institutions.

[10] https://www.gov.je/SiteCollectionDocuments/Government%20and%20administration/R%20A%20review%20of%20the%20Jersey%20regulatory%20and%20competition%20framework%2020151123%20VP.pdf

Jersey's Competition Law was introduced in 2005 and is administered by the Jersey Competition and Regulatory Authority (JCRA). As can be seen in Figure 4, this coincided with the end of a sustained period in which Jersey's inflation rate was considerably higher than the UK's. There is a significant body of research from around the globe that shows a similar relationship – that more competitive markets result in lower prices and better outcomes for consumers.

Further, increased competition has been shown to be particularly beneficial to those on lower incomes. For example, evidence from the United States[11] suggests that lower income consumers lose most from a lack of competition in telecoms while research in Mexico has demonstrated that welfare losses from monopoly power are greatest among the poor[12].

It is also possible to enhance competition in markets by increasing the information that is available to consumers to allow them to make choices that are better informed with respect to prices and product quality. The Jersey Consumer Council currently provide a number of tools, including Fuel Watch and a regular supermarket comparison of the costs of purchasing the ingredients for specific recipes.

Supporting consumers to compare prices in this way will allow them to shop around for the best deal and reduce their cost of living. Further, it has the potential to make markets more price competitive by incentivising retailers to offer lower prices in order to gain business from customers using the comparison resources.

Action 6: The Government will ensure continued support for the JCRA and will review and assess the competition framework to ensure that it remains fit-for-purpose. The Government will work with the JCRA to ensure competition policy is directed at those sectors with potentially significant impacts on the living standards of households and the competitiveness of businesses.

The Government will improve consumer knowledge by providing enhanced support to the Jersey Consumer Council to invest in existing price comparison resources and developing new comparisons across a range of different markets, starting with Grocery Watch.

[11] http://papers.ssrn.com/sol3/papers.cfm?abstract_id=296368
[12] http://www.scielo.org.mx/pdf/emne/v22n2/v22n2a2.pdf

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