



Channel Islands
Critical Mass & Economies Of Scale

Case Study Summary

Introduction

What constitutes the 'ideal island' in terms of: land area, population levels, economic profile, social infrastructure and wellbeing, fiscal performance, and climate. This question is impossible to answer but while all islands experience varying degrees of isolation, some island communities have a distinct advantage over others purely because of their critical mass and their ability to benefit from economies of scale.

These scenarios equally apply to the Channel Islands which has an overall population of 173,000 and where total public sector operational expenditure is well in excess of £1 billion annually. This is in addition to some very costly capital infrastructure projects which are either in the pipeline or being considered (e.g. new hospital facilities, secondary schools, airport rehabilitation, etc.). The archipelago also comprises four main islands only a very short distance apart, each with a separate government structure and constitution but with populations ranging from 108k down to 500.

This Summary Paper is designed to be thought-provoking by highlighting current issues facing the Channel Islands and where the adoption of 'economies of scale' policies would be most appropriate across all of the islands in meeting these challenges. Above all, the primary objective is to engender rational debate rather than 'sparking' inter-island rivalries and competing agendas.



Definitions (Island Context)

Critical Mass

In an island context, critical mass is defined as the minimum level that an island's population, infrastructure and service provision should be in order to allow both:

- social services to be at optimum levels of scale and affordability and
- the island's economy to be viable and financially self-sustaining

Above all, the island's very existence should not be reliant on external support from a neighbouring island or country. When an island reaches this critical mass, a decision needs to be taken on whether:

- it should pursue further, perhaps unsustainable, economic growth to provide ever-increasing levels of service with associated costs, or whether:
- it should focus on following a sustainable economic track with affordable on-island services.

Economies of Scale

This describes the advantage that a large island has in terms of its population size, land area, and economic profile over a smaller island community. In simple terms, the larger the island is, the lower are its unit costs and the greater is its competitiveness and efficiency.

There are two main forms of economies of scale - internal and external. Internal economies are, as the name implies, internal to the island itself and controllable by government. External economies are supported by external factors. These factors include geographic location, 'mother' country or international agency support, etc. Small more remote island groups simply do not have the leverage to take advantage of external economies of scale. However, they can work together and benefit from geographic economies of scale by clustering similar services in one location.

Sometimes an island can over-extend itself in that by chasing economies of scale, its size becomes a disadvantage. This is called a 'diseconomy of scale'. For example, it might take longer to make decisions resulting in the island being less flexible to change.

Key Historical Lifecycle Factors

A rebuilding of the economic and social infrastructure after the end of the Second World War led to a transformation of the Channel Islands as compared to pre-war conditions. Rapid growth in tourism, horticulture and agriculture attracted net immigration made up of both returning islanders and new residents.

In the 1950s and 1960s, tourism, in particular, benefited from the expansion of the UK holiday market, greater affluence generally, and cheap travel options available to British Rail employees and their families. (At the time, UK/CI passenger ferry services were owned and operated by British Rail - a public sector organisation). In addition, CI population levels, as in the UK, were also further enhanced by the immediate post-war boom in birth rate.

It was from the early 1970s onwards that things started to diverge between the islands. Therefore, 1971 is used as a benchmark year (immediately prior to the UK joining the European Economic Community (EEC)). This divergence was primarily driven by different economic factors and policies adopted by each of the Channel Islands.

Over the last half century, there have been some major events which have impacted both positively and negatively on the Channel Islands. The rate of change in population growth between the islands since 1971 can be viewed as an indicator of key economic and social circumstances at the time.

The following timeline sets these out by decade and identifies some of the significant influencing lifecycle factors. Above all, these factors will become more frequent and intense moving forward into the next couple of decades.

Key Factors

Finance sector continues to develop rapidly in Jersey and sector starts to look at Guernsey as a base. Having experienced record levels of unemployment, this is welcomed by Guernsey with major population growth as a result of new employment opportunities occurring in this island during the second half of the decade.

Both islands introduce stringent employment control measures to moderate overheating economies and net immigration.

CI tourism continues to find it difficult to compete with the growing overseas package holiday market. Jersey tourism boosted to some extent by the BBC TV 'Bergerac' series which was filmed in the Island between 1981 and 1991.

Population Change Jersey +11%

Population Change Guernsey +10%

Key Factors

As in other parts of the world, the rapid expansion of the banking sector again responsible for population growth, more in Jersey than Guernsey.

Significant strengthening of sterling adversely affects the islands' European visitor market as does growth of low-cost air transport model which does not encompass CI. This results in a major decline in the number of hotel beds.

While the 2008 financial crisis did not immediately have a negative impact in the CI, the tightening of regulation and the growth in the use of information technology results in a contraction of the sector, and ultimately, of the CI economy.

Population Change Jersey +12%

Population Change Guernsey +5%

1971-1980

Key Factors

UK joins EEC in 1973 - Guernsey's largest economic sector adversely affected by major decline of its UK market due to lifting of tariffs on flower and tomato imports into the UK. This coincides with 1973 oil crisis which saw a threefold increase in oil prices (Guernsey horticulture depended on oil to heat its glasshouses. Holland heated its glasshouse sector using cheap natural gas).

Finance sector develops in Jersey.

CI 'traditional' visitor market under threat from package holiday growth to countries such as Spain, Greece, Italy and other European destinations.

Population Change Jersey +10%

Population Change Guernsey +4%

1981-1990

1991-2000

Key Factors

The UK Economic recession during the first half of decade as well as monetary crises adversely impacts both islands.

Greater regulatory requirements introduced in the finance sector and other jurisdictions begin to enter the finance sector market attracting business in their own right.

CI tourism boosted by the very low value of sterling versus European currencies. The islands see rapid expansion of the mainland European tourism market with the introduction of many direct flights between the islands and the continent.

Population Change Jersey +4%

Population Change Guernsey +2%

2001-2010

2011-2020

Key Factors

Major contraction of CI banking sector, the further tightening of regulation, and the continuing development of IT have significant impact on CI economies. However, product diversification begins to turn round finance sector.

Merger and consolidation of many Guernsey and Jersey based companies takes place with more 'headquarter' emphasis in Jersey. Inter-island air connectivity deteriorates to the detriment of Guernsey economy. Jersey able to embrace low-cost air travel market. Jersey relaxes immigration policy.

Online shopping has a detrimental effect on traditional retail market and employment levels. Guernsey construction sector contracts due to lack of public and private sector building projects.

BREXIT vote and subsequent uncertainties create real challenges for CI governance and economies. Current COVID-19 Pandemic has long-term negative economic and social ramifications on all communities around the world including CI.

Population Change Jersey +10%

Population Change Guernsey +0%

Key Impact Factors

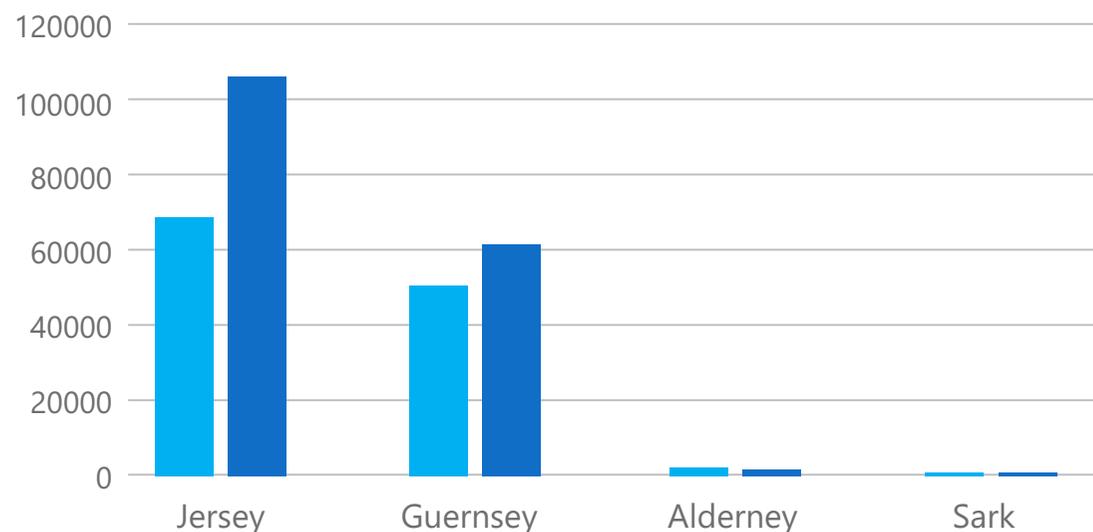
Population Change

In 2019, the Channel Islands population stood at 173,000, a 40% increase over 1971.

The population distribution between the islands has also changed significantly with 62% (56% in 1971) of the total now residing in Jersey, 37% (42% in 1971) in Guernsey, and 1% (2% in 1971) in Alderney and Sark.

Jersey's current population is 55% greater than it was in 1971 (+38.5k people) while Guernsey's population is 23% larger (+11.7k people).

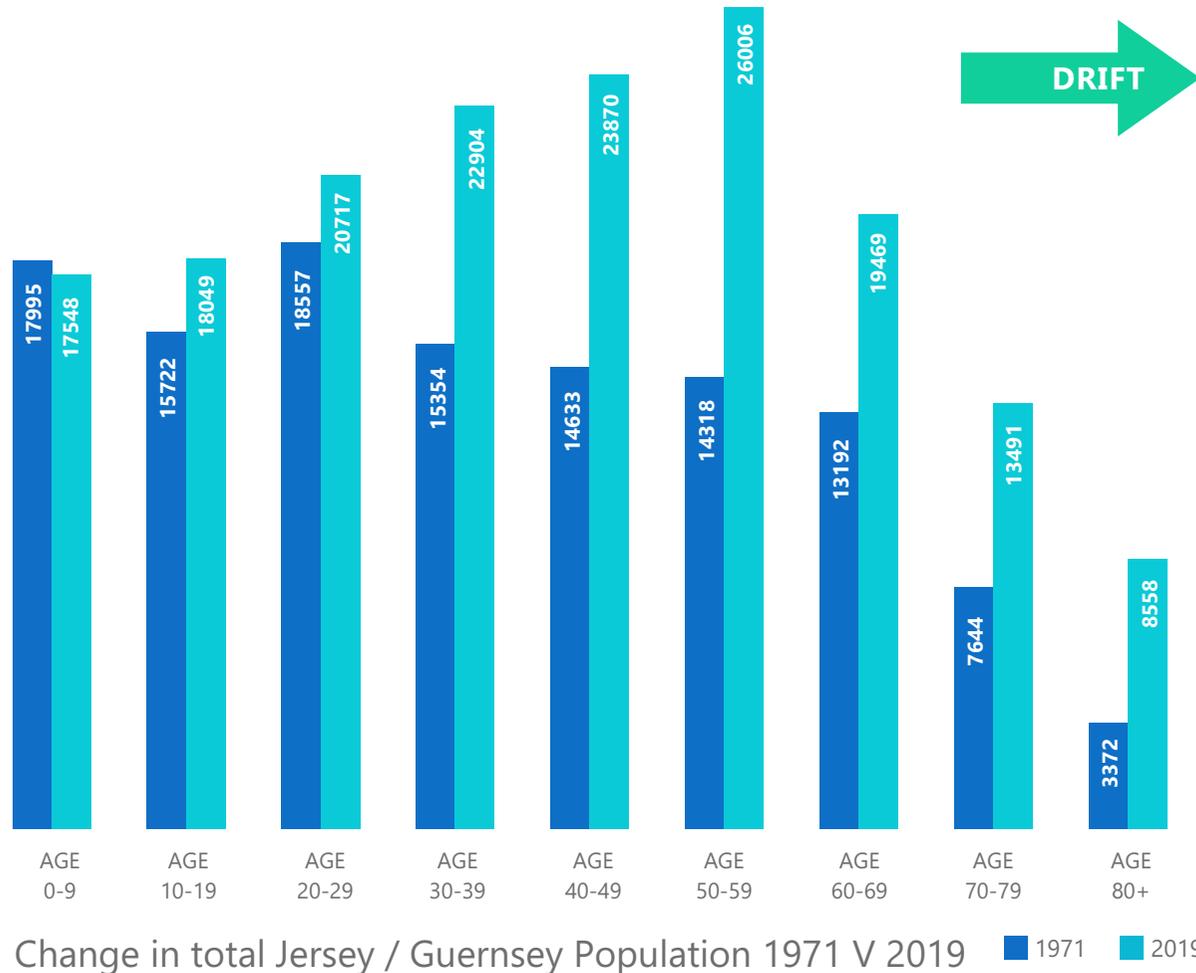
There has been no real change in the population levels of Alderney and Sark now as compared to 1971 albeit the population in these islands did increase during the 1970s and 1980s only to decline since the turn of the millennium.



Channel Islands Population Change over 50 Years ■ 1971 ■ 2019

Key Impact Factors

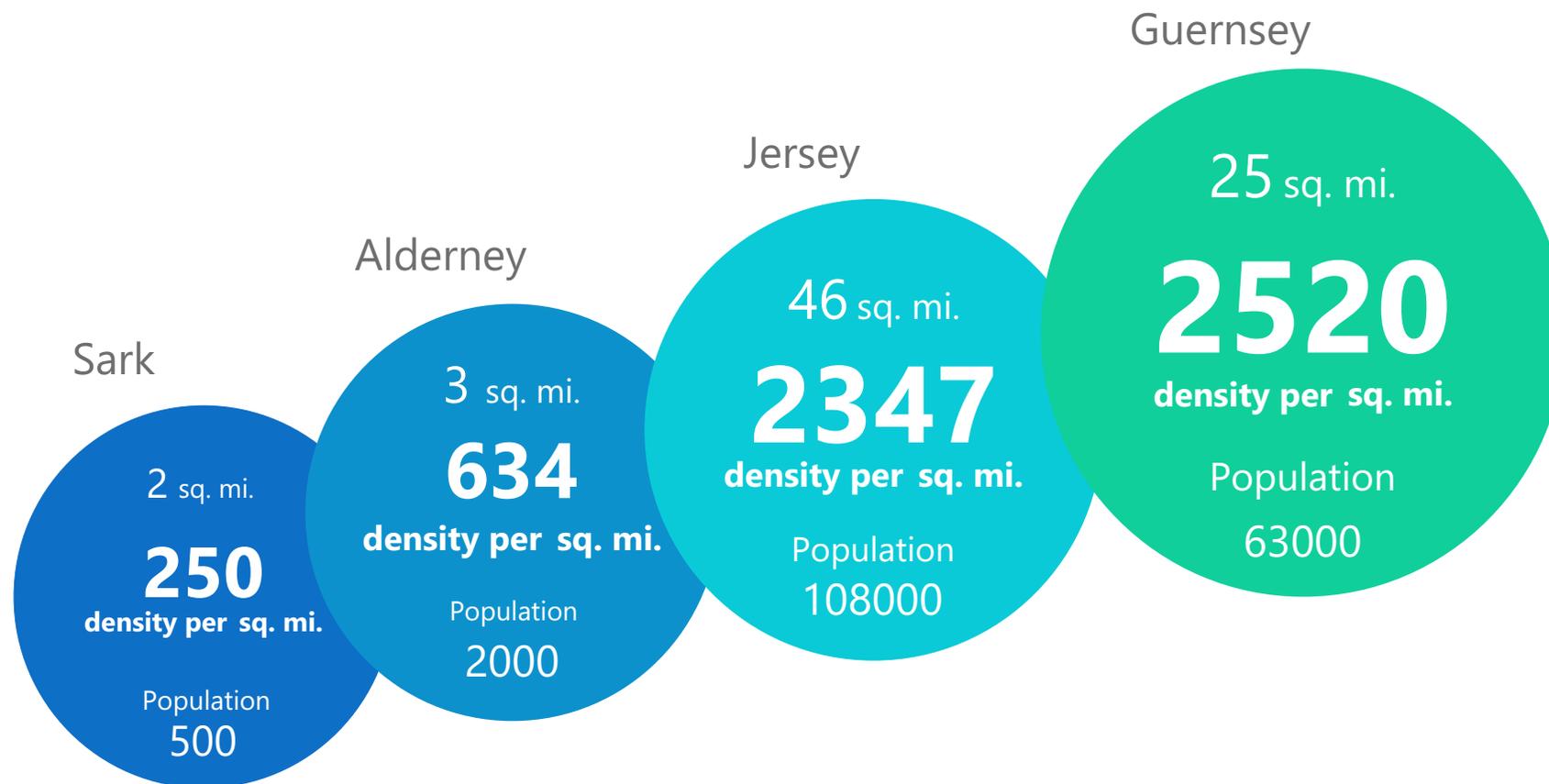
Population Age Drift



- Despite 23% increase in population over the period, there are now 3k fewer 0-19 year olds in Guernsey than there were nearly half a century ago. This is not the case in Jersey.
- 50-59 age group now represents the peak age band in both islands. There are currently 26k people in this group as compared with 14k in 1971 - a 79% increase. In 1971, the largest age group in Guernsey comprised 0-9 year olds and, in Jersey, 20-29 year olds.
- As far as Alderney is concerned the peak age group is now the 70-79 year olds.
- There are now 8.5k residents in Jersey and Guernsey who are aged 80 and over (there were only 3.4k in 1971), a 152% growth. There are a further 13.5k who are currently aged between 70 and 79 (7.6k in 1971, a 74% increase).

Key Impact Factors

Land Area and Population Density



Guernsey still remains the most densely populated community in the Channel Islands.

CI Private Sector embraces Economies of Scale

Over the last decade, critical mass and economies of scale have already been applied in many areas of the private sector within the Channel Islands.

There have been numerous businesses, particularly UK corporate organisations which have seen the merit in operating seamlessly across both Jersey and Guernsey and, in some instances, Alderney as well. However, since the 2008 financial crisis and the contraction/recovery of the finance sector in each island, companies have increasingly recognised the financial and business advantages of applying critical mass and economies of scale primarily through:

- a merger of separately owned businesses previously located in one particular island, and
- the expansion in the number of companies now operating on a pan Channel Islands basis.

This growing pan-CI trend can now be seen across all economic sectors and primarily in the areas set out in this chart:



CI Private Sector embraces Economies of Scale

In some instances, mergers and acquisitions have occurred out of necessity because of a contraction of market size and/or greater competition but other factors come into play including:

- a reduction in the quality of inter-island travel
- the growth in the use of IT and artificial intelligence
- the varying pace of economic development in each island
- the need to achieve economies of scale by providing a broader skills base within the organisation and increasing overall buying power.

However, one resultant trend is the migration of current and new business away from Guernsey in favour of Jersey as the CI hub. There are some important factors which have encouraged this to happen including:

- much better air transport connectivity to and from Jersey
- lower cost of travel to and from Jersey
- more flexible labour/immigration policies in Jersey than in Guernsey

- benefits of a greater land area of Jersey as compared with Guernsey which has enabled a rapid expansion of business premises to occur and private household accommodation to be constructed.

A number of marketing functions are still undertaken separately in each island. The three most significant are in tourism, financial services and the attraction of new business and high net worth individuals. While there are synergies within tourism (benefits of island hopping, shared external marketing promotions etc.) very little joint working occurs in the marketing of financial services.

It is interesting to note that the same company operates public transport services in both Jersey and Guernsey and receives a subsidy separately from each island.

Finally, it is important to note the growth in business being generated within the Channel Islands market as a whole by companies based in other parts of the world. A notable example is Amazon.

CI Public Sector & Economies of Scale

While the Private Sector has embraced the need to optimise the application of critical mass and economies of scale across the Channel Islands, this has not generally been the case as far as the public sector is concerned.

Given the relentless increase in costs associated with the need to resource rising public expectations on the quality of services generally, the luxury of having separately administered public services in each of the main Channel Islands becomes hard to justify. This is even more the case given the challenges that the world, let alone the Channel Islands, now faces over the next twenty years. On the other hand, the Channel Islands as a whole has a real opportunity to see where there are public sector opportunities to pursue on a pan-CI basis.

This chart sets out the external challenges now impacting and which will impact on the Channel Islands:



Challenges & Opportunities

There are many common areas between the islands in relation to external affairs, governance, economies and social infrastructure. However, despite these similarities, the two most destructive events since the World War II adversely to impact on the Channel Islands as a whole (2008 Financial Crisis and 2020 COVID-19 Pandemic) have seen Jersey and Guernsey working apart in their endeavours to address the associated challenges.

Given the ever-growing number of external threats (see previous chart) which, to a greater or lesser extent, will certainly have an impact on the CI over the next two decades, there is now a real need for a pan 'Channel Islands' vision which addresses CI economic, social and environmental opportunities and solutions going forward by taking account of critical mass and embracing economies of scale.

Such a pan-CI approach also covers the 'micro' challenges which are equally as important. Here are just four examples. However, there are many more areas which justify joint consideration and co-operation.



Ageing Population: Resource Demands



Pan-CI Flexible Employment Pool



Future Delivery of Education and Training



Climate Change and the Environment

Challenges and Opportunities

Examples



Ageing Population: Resource Demands

The number of people aged over 80 in the Channel Islands will treble (from 8k to 20/25k) over the next twenty years. This will significantly increase health costs and impact immensely on CI resources as a whole with a real danger of service duplication in each island. Another factor which is often overlooked is the need for carers which will draw economically active residents away from the work environment. A pan-CI strategy solution is only common sense.



Future Delivery of Education and Training

In terms of vision, there could well be a time when the traditional school model will change and the use of remote learning will become the norm with schools being gradually replaced by centres for 'soft skills' training. Such a change would justify a common approach across the Channel Islands particularly in the provision of e-learning facilities.



Pan-CI Flexible Employment Pool

The COVID Pandemic will only hasten changes in work practices and lifestyle choices, let alone the growth of artificial intelligence which will impact on all the islands both positively and negatively. This is arguably one the most important areas which should be dealt with on a pan-CI basis. A policy of the free movement (physically and virtually) within the CI of economically active persons should be given real thought.



Climate Change and the Environment

The ever-pressing demands of climate change issues have not diminished in any way. Again, the ramifications on the Channel Islands are significant. Three obvious impact areas are sea level rise (storm surges and flooding), water supply security, and CO2 emissions policy. Again, a common pan-CI strategy only enhances the reputation of the CI in being seen as working as one.

Contact Us

For Business Enquiries

The application of critical mass and economies of scale is not only relevant to the Channel Islands but to every small community and island around the world.

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