



Guernsey Financial Services Commission

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How the Bailiwick Enhances Global Prosperity

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Thank you for coming along today after what has been an obviously odd last year and a bit. It has been an example of a black swan event challenging an awful lot of our presumptions about how things actually work and how we do things. My focus today is going to be on economic matters, how the Bailiwick does and must continue to add value to the global economy and the role the Commission seeks to play within that rich and complex tapestry.

Trade

To start with the obvious, Guernsey is not well adapted to autarky. Its people have always made their living through trade with the world beyond our islands. The extraction of granite, the production of tomatoes and flowers and acting as a redistribution hub for Bonapartist freight in the early 19th Century, are all noteworthy examples of how trade in goods historically contributed to Guernsey's wellbeing. As we moved into the later part of the 20th Century, the nature of trade changed for the Bailiwick as for much of the rest of the world with trade in services becoming rather more important than trade in goods.

Given that the Bailiwick had, through Protocol III of the UK's treaty of accession to the European Union, locked into a very fixed arrangement optimised for trade in goods, this left the Bailiwick in a rather invidious and disadvantageous position for about 46 years. I say this on the basis that the EU, during the UK's membership, negotiated trade deals with both services and goods components. So, in summary, Protocol III meant that Guernsey could not benefit from any global lowering in barriers to trade in services negotiated by the EU with other jurisdictions because it was never part of the EU for services. Now that the UK has left the EU our chances of being able to meaningfully participate in global trade deals involving services, including financial services, are much much greater.

As of 1st January this year, the UK (or at least the UK ex-Northern Ireland) became free for the first time in my lifetime to negotiate its own trade deals in its own name. Further to that, the services trade barriers between ourselves and the UK which legally existed because it was part of the European Economic Area whilst we were not, declined markedly. What this means is that, assuming we can jump over the relevant and proper hurdles which the UK sets for our participation, as well as coming under the umbrella of the UK's World Trade Organisation membership, we can also ask to participate in new UK trade agreements with high growth countries where wealth and prosperity are actually being generated. Asia is already home to more billionaires than any other region, with 36% of the global total, and expected to see 39% growth in ultra-high-net-worth individuals over the next five years – the fastest growth in this demographic of any continent (Knight Frank, 2021).

What this means is that we are potentially, in partnership with the UK, able to enjoy better access into overseas markets for our services, for example our funds, than we were able to previously obtain. This access of course depends on us being perceived as good and grown up international partners. As Mr Bailey, the Governor of the Bank of England, laid out clearly in his speech of 10th February¹, this access, “requires us to give up some control over our standards and rules, because the alternative of a narrow domestic control is illusory – it would jeopardise achieving the very things we want, safe open markets and likewise open economies”. The Commission seeks to help ensure that Guernsey is regarded as an acceptable counter-party to important international trade agreements by ensuring that we are not just technically compliant but effectively applying, in a proportionate manner, international rules which govern how financial services firms which want to do cross border trade must conduct themselves.

To this end we continue to be active in the working groups of the International Organisation of Securities Commissions, the Financial Action Task Force, the International Association of Insurance Supervisors, the International Organisation of Pension Supervisors, the Network for Greening the Financial System, the Global Financial Innovation Network and the Group of International Financial Centre Supervisors thereby helping to prove that we wish to and can contribute as a Bailiwick to the Global commons, helping to set the standards under which international financial services trade can contribute to global prosperity. None of this is easy, but as we know, it is the victors who redraw national boundaries at the end of wars and so it is with those who put energy and effort into international fora influence the rules through which modern services trade is governed.

Economic Change in the past Twelve Months

The changes caused by the international reaction to Covid are numerous and will be the subject of many speeches for at least the next decade. Today, I’m merely going to skirt around that vast subject and offer a few initial observations about changes which may be pertinent to the Bailiwick in the relatively near term:-

- Firstly, the Bailiwick has proved in the pandemic that it is possible for its firms to do almost all their business with their international clients entirely remotely. Whilst no one particularly enjoys days of intensely draining video meetings, we have proven that international financial services can continue successfully to add value without much international travel. I would certainly not want to say that this could be a “forever” position – I know how much we all miss the physical interaction for which video meetings are a poor substitute – but it has certainly helped the Bailiwick’s IFC be far more resilient than we had thought it could be when Covid hit in March last year. Katherine Jane will provide more details later but suffice it to say that, despite the pandemic, we still had 95% of the applications of the prior year in 2020 – a testament to the resilience of the sector we regulate.
- Secondly the pandemic proved the value of having substance on the ground. Substance is, these days, important for tax reasons. It has always been important for regulatory reasons – so we could provide assurance that real people were doing proper things in a proper way. The pandemic showed how substance was important for practical reasons - connected with being able to continually service clients - when some outsourcing which had taken place to other jurisdictions was not necessarily 100% functional all the time. I hope this enhanced recognition of the need for substance on the ground will continue to contribute to high

¹ With reference to the UK itself.

employment levels within the Bailiwick's IFC. At the Commission we appreciate that there must be outsourcing and indeed we encourage it in some areas where it can increase resilience (for example to good quality cloud service providers with strong financials and strong levels of internal resilience²) that said, there needs to be a balance and, as global norms evolve, we cannot see there being much future for jurisdictions which provide no more than tax advantaged brass plates – there has to be real value added in a jurisdiction – as there is under Guernsey's economic model.

- Thirdly the nature of money has changed. Here I am not talking about the latest fork in Bitcoin or some similar derivative that facilitates the illegal export of money from the People's Republic or the latest online ransomware to blackmail innocent citizens more easily. Rather, I'm talking about the unbelievably large amounts of fiat currency which the world's major central banks have electronically printed over the last year. As at the end of 2020 we had seen the UK undertake an additional £450bn of quantitative easing in response to the pandemic, the EU an extra €1,850bn, and the US a further \$3trn (Breedon et al, 2012; Ramsden, 2021; Trichet, 2009; European Central Bank, 2020; Federal Reserve, 2021). For the UK, this is more than double the amount of QE we saw in the immediate aftermath of the 2008 Global Financial Crisis, and for the EU it is over thirty times more. The Bailiwick is very largely a buy side jurisdiction. By this I mean that it provides services for savers and investors. The big question for them will be what the creation of this global forest of magic money trees actually means for their long term welfare. Some will worry about its inflationary effects as inflation often benefits debtors rather than creditors and some will worry about confiscatory taxation at the sort of levels of which the German constitution disapproves - as unwise souls make valiant but ultimately self-destructive attempts to stuff the inflationary genie back into its bottle – as the UK tried with such adverse consequences for the wellbeing of its citizens in the 1920s. The Bailiwick's firms need to adapt to these new realities and help the entrepreneurs and savers they serve navigate these inflationary currents through the rocks of fiscal distress to hopefully calmer waters beyond. If the Bailiwick can be seen to provide a port able to preserve and enhance the productive use of savings during the coming turbulent times it can do a great service to many of those who have the intellect and energy to drive the global economic revival.
- Fourthly, the supply chains of major industries are changing and will continue to change. The pandemic has caused many otherwise apolitical people to become all too conscious of the threat that geopolitical tensions create for their supply chains and many governments, caught short in terms of both PPE and vaccine supply, are likely to require much more national supply chain resilience going forwards. Building such national resilience will require major reinvestment in what were previously regarded as backwater industries at least by us in the post-industrial West. Guernsey's private equity expertise should mean it can offer timely funding to the entrepreneurs whose rebuilding of large economies could help stave off 1930s style mass unemployment in response to the changes in the economic landscape accelerated by Covid. For our part, as my colleagues will elaborate in their presentations, the Commission has continued to refine and improve policy so the financial services sector in Guernsey can continue to evolve successfully.
- Fifthly and finally, ironically, Covid has certainly bought forward the green revolution. Within the space of 12 months, such great industrial powers as the US, China, Japan and South Korea have all signed up to net zero carbon emission targets. This has left climate

² Resilience of cloud service providers is an area in which both British and European regulators are doing much work. We will watch the conclusions they reach as to how far financial regulators need to reach down into cloud services providers to ensure systemic resilience with interest.

change sceptical business with almost nowhere left to run. The Bailiwick took a lead in 2018 on environmental finance through our Guernsey Green Fund and our firms need to consider how they can best invest to help deliver the deluge of carbon negative investment these new climate change targets mandate across the world and also whether they should be taking measures to reduce or compensate for their own carbon footprints. By this time next year we hope to be on our own way to doing so as we plant several thousand trees as part of a physical long term investment in carbon offsetting.

How Guernsey Adds Value to the Post Pandemic Global Economy

Much though I and many others much enjoyed living safely in our little Guernsey bubble during the summer months – gently sailing around Alderney and Sark - economically we are one of the most interconnected finance hubs on the face of the planet – anything but a bubble. At the Commission, we are far from naïve and know full well that some international actors and lobbyists seek to challenge our existence – indeed many of them are so carried away by their own rhetoric that they would probably sign up for global warming if they could just be assured that the melting Artic ice sheets would ensure that the Bailiwick was swallowed up by the ocean.

Their case against the Bailiwick is based upon a myth - and a selfish, self-regarding myth at that – one that is based upon a flawed understanding of both economics and human nature. It is to debunking this myth that I will devote the remainder of my talk today.

As we stand on the threshold of what we must all hope will be the gateway to restored freedom, a freedom built on academic excellence, and a strong public-private sector partnership for vaccine development and delivery, there is much which needs to be rebuilt. During the pandemic many people have suffered and for many of them the pandemic countermeasures may well prove to have been much worse than the virus itself as they have lost all that they have worked for a lifetime to build. They emerge from the rubble with the business models upon which they and their employees have previously traded, undermined and with severely impaired cash flow with which to fund rebuilding and repurposing.

In the minds of our detractors, the Bailiwick's irritating prosperity as a buy side centre somehow inhibits that rebuilding because we still have funds to invest when others have run out of money. This thesis is built on a false understanding that the world can only exist on a win-lose basis, that the size of the cake to be shared was fixed in ancient times at a preordained size. It resembles, in only a slightly modernised form, a Nietzsche-like struggle for the triumph of the will to power and we all know how that ended. As the magic money tree economics of the global central banks over the last months has shown, the supply of money is not fixed and nor is the supply of prosperity fixed. Indeed, since the early Middle Ages technological and political evolution has shown that the supply of prosperity is far from fixed. Whereas in 1000 AD almost anywhere in Europe one would simply have been able to divide people into warriors and tillers of the soil, with the odd priest thrown in for good measure), by 1300 AD advanced societies with much greater culture and prosperity existed following decades of much improved government with innovations such as the creation of prosperous monastic centres and universities. This has continued, with lamentable lapses caused largely by mistakes in governance, across our European continent ever since. The stock of prosperity is not limited. The Bailiwick's prosperity is not someone else's poverty – quite the reverse. x2

To take a relatively modern analogue, in 1997 when Hong Kong was handed back by the British to the People's Republic, despite being smaller than West Sussex, it comprised 18% of the GDP of China³ (World Bank, 2021). China was desperate to have it back, not just to close a chapter on the Opium Wars but because it understood that the supply of prosperity was not fixed and how Hong Kong's commercial and financial expertise could supercharge its own growth – as indeed happened over the following twenty years. That this was the case was because for the previous few decades, Hong Kong benefited from unideological, pragmatic, honest and competent British public administration. x2 Deng Xiaoping understood what value that offered China when he took over from Mao and tried to inculcate a Chinese renaissance. Hong Kong island, a rock almost exactly the same size as the island of Guernsey, helped turn around the fortunes of the world's most populous nation. Deng Xiaoping understood that prosperity wasn't fixed but something to be generated by good quality government combined with good quality entrepreneurship by a hardworking and well educated population.

Guernsey does not operate on the scale on which Hong Kong once operated but as the world seeks to rebuild from the pandemic, we offer many services to the rest of the world which can help it generate greater economic and societal wellbeing:-

- We provide a secure home for patient capital. We all know that quarterly results reporting, backed by business buzzword bingo, are not the underlying drivers of prosperity. Rather patient capital is required to undertake long and experimental investments which may take many years to show a good return. For capital to be patient it needs to be secure, for who would invest if they thought that any benefits from their risk taking would be taken from them whilst the losses would be merely their own. x2 The Bailiwick provides just such a secure home that encourages such risk taking for longer term investment.
- We offer a safe environment in which financial services firms can interact. Who wants to take risks with their money when it might easily be taken from them through an arbitrary sleight of hand “might is right” move by a competitor or supplier. Here our laws, backed by well attuned judges at the Royal Court and the Commission's “policing the beat” supervisory activities, make that far less likely to happen than in other jurisdictions whilst our enforcement activities should give other jurisdictions confidence that investments from the Bailiwick are untainted.
- We offer a great, tax transparent, low bureaucracy environment in which to pool the funds necessary to take risks on big economic ventures. Relatively few other domiciles can offer the expertise the Bailiwick can pull together to gather funds and then deploy them on gainful real world projects in a sensibly risk adjusted way. Our detractors like to pretend that all the projects which Guernsey's financial services sector funds across the world would somehow magically happen anyway if the Bailiwick wasn't there to pull all the pieces together and make the societally beneficial economic activity happen. That is more than a little tendentious. If we and our cousins in Jersey were not about to pool together capital from around the world in a lawful and pragmatic fashion, much investment and prosperity might well simply not happen. In the same way that there is not a fixed global pie of prosperity, there is not a fixed global supply of flour, yeast or baking powder to grow the pie. X2 At a time when many decent individuals and their real world companies will need recapitalisation to recover, Guernsey's large private equity and private capital sector has considerable dry powder to deploy to grow the size of other jurisdiction's pies, dry powder which there is no good reason to think others would be able to produce or deploy as well as Guernsey.

³ In 1996, the GDP of Hong Kong was \$160bn relative to China's GDP of \$864bn, measured in current US\$.

- We offer carbon negative investment products and advantageous regulation for insurers seeking to make green investments to build a more environmentally secure future. Whilst others are thankfully also active in this field, given the trillions of pounds of investment required to make the Paris Climate Change Agreement targets a reality, we stand well prepared to more than pull our weight to help other jurisdictions move fast towards the carbon neutrality most scientists think would be strongly in our children's interests.

What the Commission, alongside other local official sector actors, seeks to offer is much the same as that which a prior generation of British public servants offered the people of Hong Kong and the surrounding countries during the turbulence of the Cultural Revolution: pragmatic, sensible, principled but unideological British public service. At a time when too much ideological thought on both the left and the right seems intent on putting humanity into arbitrary groups who are assumed to be in perpetual conflict with one another, we treat people as individuals and judge them on their merits. We believe in one rule of law under the Crown for all people irrespective of their class, race, gender or any other supposedly "defining" characteristic. We don't care if you are rich, locally schooled and incredibly well connected – if you break the law and launder money, rip off the vulnerable and endanger financial stability, we will take robust action to protect all the others who depend on Guernsey's eco-system. We are interested and receptive to beneficial technological innovations whilst remaining profoundly sceptical about pseudo innovations surrounded by marketing buzzwords which appear to us only likely to enrich the promoter at the expense of retail investors who would be likely to lose their shirts. We are anxious to facilitate green investment whilst keen to avoid greenwashing by those out to make a fast buck at the expense of the credulous and well intentioned.

In saying these things and making these assertions about how Guernsey contributes positively to the global commons, I would love, for the sake of the humanity we share with other nations, to claim that we are nothing very special because, were I able to do that then the lot of humankind would be much better than it is for so many in our troubled world. We see tectonic plates moving in the global order. We see many challenging and fundamentally unkind and unintelligent ideologies rampant in the face of these shifting tectonic plates. We still believe and apply the enlightenment values of liberty, progress, tolerance, fraternity and constitutional government. We trust that both the business community and the much wider global citizenry who use their services will find our continued application of those values continues to enable human progress as those values have consistently done for many centuries.

We may well get things wrong from time to time. We have no illusions of infallibility and lack the thoughtless zeal of the mindless ideologue, so we like to think we can learn and get better when we get things wrong. Further, we hope we can help through practical, effective and pragmatic public administration - based on common sense and decency. In this way we believe we can continue to contribute productively to the Guernsey ecosystem, helping you to play your proper role - contributing to rebuilding prosperity in other jurisdictions.

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