Efling - Trade Union

Kjarafréttir

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The economists of the National economic council now say that there is no possibility for raises, because of high inflation in the world economy. This is misleading. Raises are made possible by growth in GDP and productivity. Both are in good order in Iceland this year, and the earnings of most companies are good.

The elites have taken large raises, bigger bonuses and more stock options. Dividends are at a maximum and capital gains to top earners have risen enormously. In addition, they have gotten tax concessions.

It is a bare minimum to let workers enjoy the fruits of their productivity increase with a corresponding increase in purchasing power. If not, then the income distribution will be tilted even further toward the highest earners and biggest owners. There is plenty of reason for workers to get a better deal and the beneficial experience of the 2019 collective agreement model shows us the best way to take in the current conditions. This will be further detailed below.

This analysis is based on given conditions, but the demands of Efling are exclusively made by its negotiations committee.

The why and how of raises in 2022

I. Introduction: Must inflation be fought to labour's detriment?

Inflation is at high levels compared with the last decade. This is due to temporary effects of the covid pandemic on international supply chains, and because the war in Ukraine has raised oil and food prices. Both are temporary imported factors affecting inflation. National instruments of economic policy won't affect them. Lower purchasing power of Icelandic wages won't stop the war in Ukraine, nor will it lower oil and food prices on world markets.

The local causes of inflation are especially the rapidly rising housing prices, which can be traced to the economic policy failures of the central bank in 2020 and 2021. Rapid rate hikes in 2022 are meant to decrease demand for housing by making loans dearer. That action won't hit only those who are planning to buy real estate, but everybody with a mortgage. Thus, this is a highly non-specific strike that hits the great majority of workers, to little effect. Higher interest burdens for households are already costing regular families tens of thousands each month, eroding their purchasing power – as does inflation.

Inflation of the current type does not justify wages dropping behind inflation, unless people want to use the opportunity to rob workers of the national productivity increase. Efling rejects that idea tout court, there is no excuse for it as things stand. Imported inflation will probably abate as soon as next year, and with an expanding housing supply, real estate price rises will slow down.

There is no need for lower wages or lower purchasing power. Iceland already has Europe's highest cost of living, alongside Switzerland, and raises are necessary for workers to keep up with inflation.

II. Raises

Normally, the reasoning for raises is above all else about GDP growth in excess of population growth – productivity growth. To maintain the distribution of incomes, the purchasing power of wages must rise by as much as productivity. The statistics office projects 5.1% GDP growth in 2022, and we may expect a 3% population increase. This would mean a 2% productivity growth in 2022, which is the same as average private sector productivity growth from 2011-2020 (cf. Arnaldur Sölvi Kristjánsson and Róbert Farestveit, **Launaþróun og framleiðni**, í *Vísbending* no. 6 2022).

The projected inflation for this year, according to StatIce, is 7.5%. For higher productivity to result in higher purchasing power for workers, **wages must rise by 7.5% + 2%, or about 9.5%**. If the inflation or GDP projections change, these preconditions will change in accordance with them. If inflation ends up being higher this year, raises must be correspondingly bigger. If it is lower next year, then the nominal raise can be lower than in 2022. Raises thus follow inflation, but do not push it forward – since inflation now is for reasons unrelated to wages.

The experience of flat raises across all wages in the 2019 collective agreement was good. Such raises lead to the greatest increase in purchasing power for the lowest paid, and a considerably lower one for those over the average wage. On image 1, we see a calculation along the lines mentioned above, with a 2% productivity increase being fully transmitted at 550 thousand per month (i.e., a 9.5% raise), and keeping the purchasing power of the average wage intact (i.e., at 700 thousand a month, the raise is equal to inflation, at 7.5%).

This corresponds to a flat raise of 52,250kr/month. That is similar to the 2019 collective agreements, but at a higher level of inflation. This method leads to higher increases in purchasing power for the lowest income groups, less for those higher up, which partly shields business from the increase.

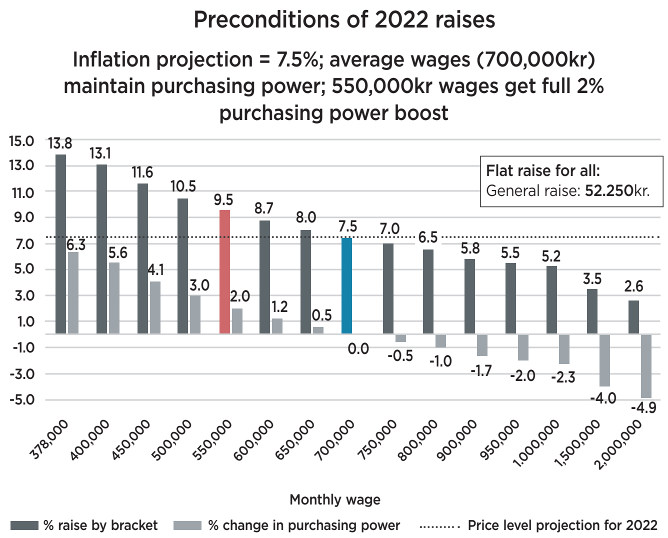

Image 1 Preconditions for raises, assuming 7.5% inflation and 2% productivity growth in 2022. The raise will be flat, 52,250kr/month. The image shows the proportional raise and change in purchasing power for different wage brackets.

The raise on the minimum wage (378,000kr) would be 13.8%. Those with the very highest wages would fall behind inflation and their purchasing power be reduced. These numbers would change if the preconditions change, upwards or down. If inflation ends up being 10% in 2022, a 66,000kr flat raise would be required to get the same real values as in the example above.

Self-evidently, the course set in 2019 should be continued, by bringing the basic shift pay closer to actually paid wages, by raising their rates over and above the general raises. This would generally not entail any extra costs for companies.

This method of raises would reduce the effects of raises on companies, since the higher paid groups would get a proportionally smaller raise and the lower paid groups would get a proportionally bigger increase in purchasing power – where it is most needed (cf *Efling economic analysis*, no. 4, Low-wage households running at a loss).

III. The government's part

The government contributed over 80 billion kr to the 2019 collective agreements, according to its own estimates. The biggest item was to lower income taxes, by adding a low-wage bracket. Now, the government is in good shape, despite the pandemic. In fact, it is unusually good among western states. There is good reason to go the same route in the coming agreements. The following is a list of important items for workers to get government input on, to help keep the raises moderate.

III.1. Lower income tax on low wages

The government played a game of eroding the tax-free allowance most years from 1991 to 2019, which increased the tax burden on the lowest paid more than others. This reduced the gains of private sector collective agreements. In the 2019 agreements, a negotiation with the government led to lower income taxes, especially for the lowest wages, to roll this unfortunate development back. The tax burden dropped by as much as 10,000kr/month, the effective equivalent of a 15,000kr raise. That way, the gains in the agreements were protected in a way they often weren't in 1991-2019.

It is in the interests of workers to continue along this path. Inflation means the tax relief should reach 15,000kr where it's greatest, and fade out on its way up the wage scale. This can be achieved by lowering the lowest income tax bracket, or by a tax-free allowance linked to income. The costs can be financed by a higher tax bracket on wages over 1.5 million a month, and by raising capital gains tax to the level of income taxes. Other methods are available.

III.2. Housing support

It is the government's responsibility to ensure there's sufficient supply of residential housing in the country, and they have promised this, even if these promises have been kept with varying diligence. For the labour movement it's most important for the housing-related transfer programs to protect workers from great leaps in housing costs. Those systems are interest relief and the rent subsidy. Other fixes do carry some weight, too.

The government abolished the social housing system in 1999. This was a terrible mistake, as we've since seen. Prices have risen much too fast and the supply of residential housing has been too unstable and not in accord with need, especially for the lower income groups. The government's bears great responsibility in this field and it is important for housing support to be strengthened and for social housing to be constructed with more vigour.

III.2.1 Rent subsidy, rent cap

Rent has risen more in Iceland than in other European countries in the last 10 years. The rent subsidy hasn't kept up. The 10% hike in the subsidy last spring was a step in the right direction, but too little, given the extent to which rent has risen. Too many tenants suffer from excessive housing costs (cf *Efling economic analysis, no. 6*: The abject condition of tenants). The rent subsidy must be raised further.

It is also imperative for the promise given alongside the 2019 collective agreements – to restrain rising rent, e.g. with a rent cap – to be fulfilled as soon as possible. The same goes for the promise to establish a secure basis for a tenants' association.

III.2.2 Interest relief for lower income groups

In recent years, interest relief has dropped precipitously, and almost been phased out, while home prices have risen abnormally rapidly (cf *Efling economic analysis, no. 2*: Housing costs rise – interest relief falls). In place of interest relief, the state offers those buying a home to use their own private pension savings tax-free to pay down their debt. This is an action of greatest benefit to those already well off. By ruining the interest relief system, low- and middle-income groups have been robbed of their housing support while the higher income groups keep support of that kind. This is unwise and unacceptable.

Now, as young people and tenants need to go into ever deeper debt to buy a home, there is a dire need for support to low- and middle-income groups in a form well suited to a reformed interest relief system. The funding of interest relief to low-income groups needs to be increased five-fold, at the very least.

III.2.3 Capital contribution for social housing

In 2016, a social housing system of sorts was established via subsidised rental housing, with capital contributions from the government and municipalities, at the urging of labour. This is a good addition to the system but is of use to too few and can't make up for the lack of interest relief or rent subsidies. The need is dire, and the government has ample reason to contribute more in this field.

III.2.4 Lowering the impact of higher house prices on the CPI

The rise in house prices leads to a higher consumer price index, which raises household debt burdens. The central bank policy rates are then raised to reduce inflation, which further adds to the burdens. It is important to cut this vicious cycle of price and debt increases. Limiting the use of indexed loans is one route. Another is to include housing costs more softly in the index, by using a longer-term average than now. This is a change that could reduce the effects of housing market swings on inflation, an urgent matter for many reasons.

III.3. Child benefits

In the *first volume of Efling economic analysis* (Child benefits are too low), it was demonstrated that the condition of families with children is bad in Iceland compared with other Nordic countries and other western OECD countries generally. Even if the full benefits are comparable to the other Nordic countries, they are means-tested as soon as income rises above the minimum wage. Few people working full-time in Iceland thus get the full amount in child benefits. Expenditure on these benfits is also comparably low in Iceland, despite a high proportion of children in Iceland.

This means that families with, e.g., income between the poverty line and the average wage, get much less in child benefits in Iceland than in neighbouring countries. This has to be fixed now, perhaps by eliminating means testing below the average wage. This would entail a doubling of child benefits expenditures.

IV. Social security

The general pension funds were founded via the 1969 collective agreements to raise pensions. As they grew stronger and started paying higher pensions, the government increased its cuts to social security, with ever more force, right up to the present. This has hurt the pension system and prevented workers from getting the fruits of these funds as originally planned. Too many pensioners have lower wages than they should, despite the pension funds being among the biggest in the western world, as a share of GDP.

The simplest way to fix this is to raise the cap on income from pension funds before means testing begins on social security payouts – from 25,000kr a month to at least 100,000kr. The gross cost would be 15 billion, the net cost, after taxes, 10 billion.

V. Other

Various other actions could be taken to good effect. The government could cool inflation by temporarily lowering petrol/diesel fees and by lowering the VAT on food.

It is also important to continue actions against social dumping and to implement fines on those who break collective agreements.

Housing needs further rapid and broad action, like that indicated in the National economic council's housing group's proposals, recently made public.

Lastly it is very important to greatly reduce tax evasion. Light handed discipline relating to tax returns of firms in Iceland has been shown to lead to greater loss of tax income than in most other Western nations, according to recent international research. Reform in this area is needed to improve financing of the welfare state and other infrastructure of the society."

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