

The cost of Government measures to support the wage agreements reached by the social partners in April ranges up to an estimated 80 b.kr., according to a statement from the authorities. That expense will accrue over the term of the agreements, which is three years and seven months. The measures are laid out in 45 items and are therefore extensive. The main emphasis is on increasing households' disposable income and making it easier for certain groups – young people and lower-income households in particular – to enter the housing market.

Measures to increase disposable income

The income tax system will be changed to include a new low-income bracket. This will increase disposable income most at the 325,000 kr. threshold between the two lowest tax brackets, or by as much as 10,000 kr. per month. In addition, child benefits will increase by 16%, and means testing will be eased. The bulk of the expense lies in these two measures, which cost just under 66 b.kr. The fiscal plan presented by the Government in March had already assumed expenditures of 63 b.kr. in connection with these changes.

Home purchase measures

The authorisation to allocate a portion of third-pillar pension savings tax-free to mortgage loans, which has been in place since July 2014, will be extended for two years. In addition, first-time home buyers and those who have not owned property for five years are authorised to shift up to 3.5 percentage points of the pension contribution previously allocated to mutual pension funds to their third-pillar pension savings and use it, tax-free, towards a home purchase. In addition to these two special options for third-pillar pension savings, the authorities intend to work with the social partners to find mortgage loan options that make it easier for young people and low-income earners to buy their first property.

Other measures

The authorities intend to work towards reducing the importance of price indexation in the credit market. Legislative amendments are to be made so as to limit the maximum term of inflation-indexed annuity loans to 25 years and to base new indexed loans on the CPI excluding housing. There are numerous other measures, but the bulk of their cost stems from lengthening childbirth leave to twelve months.

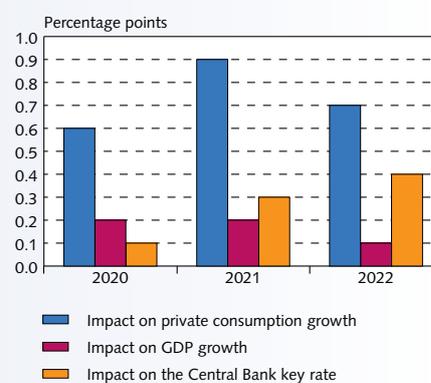
Macroeconomic impact of the measures

Reducing taxes and increasing financial support to households will increase their disposable income, thereby boosting demand for goods and services. On the whole, the measures aimed at increasing disposable income are estimated to cost 20 b.kr. in 2020 and about 25 b.kr. per year in 2021 and 2022, which translates to about 0.6–0.7% of GDP per year. These measures can be expected to increase private consumption growth by $\frac{3}{4}$ of a percentage point per year, on average (Chart 1). The impact on GDP growth is smaller, however, or about 0.2 percentage points per year, as some of the increased spending will be directed towards imported goods and services. The fiscal measures will therefore boost demand. As a result, a smaller monetary policy response to the negative shocks that have recently hit the economy will suffice. In 2020, the Central Bank's policy rate will therefore be marginally higher than it would have been without the measures, but by 2022 it will be nearly $\frac{1}{2}$ a percentage point higher.

Box 3

Fiscal measures in relation to the new wage agreements

Chart 1
Economic impact of Government measures in connection with wage agreements



Source: Central Bank of Iceland.