All rise

Automatic wage increases in collective agreements in Europe

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Stan De Spiegelaere

> *"We are heading for trouble for the simple reason that big business and monopoly industry are robbing the American public by high prices and inflation, and they are milking the most scandalous profits out of our people that have ever been known in the history of the nation. Prices and profits are up in the stratosphere, and purchasing power and real wages are being depressed more every day. Unless we get some balance in this economic machine of ours we are hell-bent for another depression."*
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> — Walter Reuther, president of the United Automobile Workers, 1947

After experiencing years of low inflation, Europe has been grappling with a sudden surge in living costs since 2021. While the inflation rate had long remained below 2%, in 2021 it rose sharply, exceeding 10%. Although analysts predict that inflation will decrease in 2023, it is likely to remain higher and more unpredictable than in previous decades (Ius Laboris, 2023).

Several factors have contributed to this inflationary trend, including supply-chain disruptions due to the COVID-19 pandemic, rising energy prices following the Ukraine conflict, and the increasing corporate profits.

However, the ramifications of the rapid rise in prices have been significant. Many countries have witnessed a massive decline in real wages, as salaries have either remained static or risen at rates below inflation. While research on the subject is still ongoing, projections and estimations indicate a substantial impact of inflation on material deprivation and poverty in Europe (Balint, 2022).

Collective bargaining has long been recognised as the traditional instrument to ensure decent wages and wage growth. Through trade unions, workers negotiate with employers to establish working standards in a particular company, industry, region, or country. The European Union (EU) has recently confirmed the importance of collective bargaining by adopting the Directive on adequate minimum wages. This directive mandates that a large majority (80%) of workers must be covered by a collective agreement, and countries failing to meet this threshold must take action to make progress towards it.

However, during times of high and unpredictable inflation, collective bargaining faces a significant challenge, as it typically enshrines wage developments for a specific period, usually at least one year. In such a scenario, if inflation turns out to be much higher than anticipated, workers may see their real wages depreciate for a certain period, which could be detrimental to their standard of living.

A potential way to address the challenge of wage depreciation during times of high inflation is through the implementation of (semi-) automatic wage increases linked to inflation, which are negotiated in sectoral or company-level agreements. These systems are often referred to as **'automatic wage indexation'** or **Cost-Of-Living Adjustments (COLA).**

By including such clauses in collective agreements, wages are adjusted to future inflation rates, providing wage rigidity in real terms and flexibility in nominal terms. In contrast, the absence of wage indexation allows for wage flexibility in real terms but rigidity in nominal terms.

During periods of higher inflation, wage indexation systems or COLA clauses become increasingly popular in collective agreements. Trade unions are now pushing for such clauses in collective bargaining rounds. To gain insight into the current state of wage indexation systems in collective agreements, **UNI Europa** (The European Services Workers Union) conducted an affiliate survey and desk research. The survey collected responses from 30 unions across 16 EU countries.

It is important to note that this text does not reflect a position of UNI Europa regarding the desirability of wage indexation systems or a preference for a specific type. The text only aims to document existing experiences and promote mutual learning regarding collective bargaining.

Wage adaptation clauses: from omnipresent to a rarity, and back

Wage adaptation clauses, such as cost-of-living adjustments (COLA) or automatic wage indexation systems, have had a varied prevalence in collective agreements throughout history.

In some European countries, such as France, Denmark, Italy, the Netherlands, and Romania, broad indexation systems were once common, but have recently declined in prevalence.

In other countries, such clauses were often included in company and sectoral level collective agreements, but have also declined in prevalence over time. Spain saw a decline from over 70% of workers being covered by an indexation clause in the early 2000s to roughly 14% in 2014-2021 (Banco De Espana, 2022, p. 56).

Also in the US, about 60% of workers covered by large collective agreements had COLA clauses in the period between 1976 to 1981, but less than one-in-four were covered by 1995 (Ehrenberg *et al.*, 1983; Hendricks and Kahn, 1982; Ragan and Bratsberg, 2000).

Similarly, in Canada, 20-30% of collective agreements included automatic COLA clauses in the 1980s, but this proportion declined significantly in the 2000s (Employment and Social Development Canada, 2015).

The prevalence of wage adaptation clauses tends to correspond to periods of high and unpredictable inflation, as trade unions prioritise the need to adapt wages to inflation. Conversely, when inflation is low and predictable, these clauses are often seen as less important and may be traded-off against other benefits.

Given the current period of high and unpredictable inflation, it is possible that Europe and the world may see a **rennaissance** in the prevalence of wage adaptation clauses, including indexation or COLA clauses, in collective agreements.

1 Types of wage indexation systems

This study has revealed that a significant number of EU countries incorporate various wage indexation systems into their collective agreements, with a growing trend towards doing so. These clauses or systems can be distinguished based on several key characteristics.

Legal basis: firstly, in some countries, indexation systems are established through legal provisions (such as in Malta and Cyprus), while in most others, they are implemented through collective bargaining agreements at different levels.

Scope: another distinguishing factor is the scope of the wage indexation system. In some countries, there are general systems in place where almost all wages are adjusted for inflation, such as in Belgium, Malta, and Luxembourg. Other countries, such as Spain and Cyprus, have a significant proportion of workers covered by such systems. However, in most countries, only a limited number of workers benefit from wage indexation systems. In Sweden, Denmark, Finland, and Germany, these systems are virtually nonexistent.

Coverage: the coverage of the indexation system may also vary. Not all systems provide full coverage of inflation, and three general types can be distinguished:

(i) automatic wage indexation **on top of** the negotiated wage increases, which is the case in some companies and in Belgium.

(ii) all-in agreements that **include** a certain wage increase that takes inflation into account. However, if inflation turns out to be higher than expected, wage adaptations will follow the inflation rate.

(iii) all-in agreements that include an inflation adaptation that is **capped**. In this case, an agreement might specify a 3% increase, but if inflation is higher, the increase will be higher, though it may be capped at, for example, 5%. If inflation is 6%, workers will still receive a 5% increase.

Different systems, different impact

The impact of different wage indexation systems can vary depending on different scenarios. In the table below, the first column represents **three different systems**. The second column includes various **negotiated wage increase scenarios**. The third column represents different **inflation scenarios**, and the fourth column shows the **resulting wage adaptations** or increases under the different scenarios and systems.

For the first system (**indexation on top of negotiated wage increase**), negotiated wage increases are assumed to be lower than in the other systems. In a scenario of low inflation, this means wage increases will be relatively low, but when inflation is high, this system leads to high wage adaptations.

Under the second system (**all-in agreements including indexation**), collective agreed wage increases are assumed to be higher. In a scenario of low inflation, this would result in real wage increases. However, when inflation is high, this system ensures wage stability but no increases.

The third system (**all-in agreements including a capped indexation**) functions similarly to the previous systems, as long as inflation is not extraordinarily high. In such a scenario (in our example, a wage increase of 4%, an indexation cap of 2%, and inflation of 10%), real wages will be depreciated.

Table 1 - wage indexation mechanisms under different inflation scenarios

	Negotiated wage increase	Inflation scenarios	Resulting wage adaptions
Wage increases on top of inflation	1% 1% 1%	2% 5% 10%	3% 6% 11%
All-in agreement + indexation	4% 4% 4%	2% 5% 10%	4% 5% 10%
All-in agreement + capped indexation (2%)	4% 4% 4%	2% 5% 10%	4% 5% 6%

Automatic character of the adaptation: while most systems involve an automatic wage adaptation tied to inflation, some agreements have a lighter system that automatically reopens wage negotiations when inflation crosses a certain threshold. In the first system, there is a guarantee for wage adaptations, but in the second, the resulting wage adaptation depends on a compromise made during renegotiation.

Reference index of inflation: the reference index used to measure inflation can also vary. Most clauses refer to national consumer price indices (CPI), but sometimes wages are adapted to other indexes. For example, in Belgium, wages are linked to a special 'smoothened health index' that takes the running average of the inflation of a basket of goods excluding highly volatile (e.g., gas and gasoline) or unhealthy (e.g., cigarettes and alcohol) products.

Forward or backward-looking: forward-looking indicators use inflation forecasts and incorporate them into wage negotiations. In contrast, backward-looking systems adapt wages to current or observed inflation. In some cases, the two approaches are combined, with previous errors in forecasts being corrected.

Timing of adaptation: lastly, there is considerable variation in the timing of wage adaptations. In some cases, wages are adapted at regular intervals (e.g., once or twice a year), while in others, they are adapted when inflation crosses a certain threshold value (e.g., a 2% rise).

2 Examples

2.1 General wage indexation systems – Belgium

In several countries including Belgium, Luxembourg, and Malta, a general system of wage indexation is in place.

In **Belgium**, sectoral agreements detail how wages should adjust to inflation. Due to the almost 100% collective bargaining coverage rate and state-facilitated sectoral bargaining, nearly all Belgian workers have some form of automatic wage adjustment to account for inflation.

However, unlike other countries that use the Consumer Price Index, wages in Belgium are tied to a custom "**smoothed health index**". This index is established in several steps. In a first step, a general price index is calculated measuring the price evolution of a selection of products. In a second step, a number of non-healthy items like tobacco and alcohol as well as volatile products like petrol are removed from this to obtain the **health index**. Then, the health index is smoothed by averaging the price increase of the past four months. This smoothing process is intended to prevent sudden price hikes from leading to abrupt wage increases. In practice, the smoothing effect slows down the wage indexation process.

The indexation of wages is not provided for by law, but is included in collectively agreements. Typically, there are two types of adaptation systems used in sectoral negotiations: (a) periodic adaptation of wages and (b) pivot index. **Periodic adaptation** involves adjusting wages at regular intervals, usually once or twice a year, based on rising living costs. The amount of adjustment depends on the inflation rate, which can be significant, small, or even negative, although negative adjustments are not typically implemented. The **pivot index** system, on the other

hand, changes wages whenever the index has increased by 2% from the previous indexation. At that point, wages increase by 2%. This system allows for a predictable increase in wages, but the timing of the adjustment depends on the rate of inflation. In some cases, the adjustment may occur relatively quickly, while in others, there may be a longer wait between two wage indexations.

Notethat the presence of almost universal automatic wage indexation systems is significant because it limits the potential for additional collectively agreed wage increases. Moreover, to prevent wages from increasing faster than neighboring countries, there is a legally binding maximum wage increase (next to the indexation) in Belgium, known as the wage norm. For the past decade the wage norm has remained low, around 1%, and is expected to remain low for the foreseeable future.

In contrast, some countries that previously had general systems of wage indexation have since abandoned them in recent decades. They include the Netherlands (1982), Italy (1993), France (1983), Denmark (1982), and Romania (2011).

Example from Belgium – Pivot index system in the retail sector

Article 2 - The minimum wages set by the collective agreement of 21 September 2015, as well as the wages actually paid and the Christmas bonus, are linked to the health index figure, determined monthly by the Federal Public Service Economy and published in the Belgian Official Gazette. (...)

Article 4 - Minimum wages and wages actually paid fluctuate by 2% each time the arithmetic average of the smoothed health index of the last three months fluctuates by 2% in relation to the pivot index. This pivot index plus or minus 2% becomes the pivot of a new stabilisation bracket. (…)

Article 5 - Increases and decreases in wages are applied from the first month following the month in which the average of the index causing the increase or decrease in wages relates.

Example from Belgium – Periodic adaptation in the banking sector

Section IV - Linkage to the consumer price index consumer prices

Art. 7 - The amounts of the wage scales shall be linked to the evolution of the health index, determined monthly by the competent federal government department.

The adjustment takes place every two months by a percentage equal to the percentage change in the arithmetic average of the health indexes of the four preceding months, compared with the arithmetic average of the health indexes of the third to the sixth month prior to the adjustment.

2.2 Partial indexation systems – Spain and the Netherlands

In several countries, there are no general systems of wage indexation, but some sectors or companies include (semi-) automatic wage indexations in collective agreements. These countries include Spain, France, the Netherlands, Romania, Turkey, Ireland, and Italy.

Trade unions in both **Spain** and the **Netherlands** are actively campaigning to generalise automatic wage indexation systems through sectoral and company-level

agreements. In Spain, collective agreements sometimes include clauses that link wages to inflation. These clauses, known as "**wage guarantee clauses**", have become more prevalent with the rising inflation. In 2022, roughly one in four collective agreements concluded in Spain included such a clause, according to incomplete data from the Spanish national bank.

Interestingly, between 2001 and 2007 roughly, over 70% of workers in Spain were covered by a collective agreement with an indexation clause. However, with the drop in inflation, the prevalence of such agreements also declined to roughly 14% for the period 2014-2021 (Banco De Espana, 2022, p. 56).

An analysis of the clauses has shown that most wage guarantee clauses envisage a yearly adaptation of wages to inflation. A minority envisage adaptations based on multi-year inflation (the length of the agreement). Additionally, most clauses (75%) include a cap or threshold. The threshold means that an adaptation will only occur when inflation is higher than a certain value, while a cap means that the adaptation is limited to a certain value (even if inflation turns out to be higher). Both mechanisms limit the extent to which wages are fully adapted to inflation.

Example from Spain – wage revision clause

For 2020, the initial wage increase to be applied to the 2019 wage tables shall be 1.5%. In the event that the resulting CPI at 31 December 2020 is higher than 1.5%, the wage tables shall be increased, as from 1 January, by the same percentage by which the said 1.5% is exceeded. The resulting difference shall be paid between February and March in a single payment.

Example from Spain – conditional wage revision clause

For the year 2024, a wage increase of 2% of the minimum wage of the agreement is agreed and for that year a wage revision clause equivalent to an additional increase of 0.75% is agreed, provided that cumulatively in 2023 there has been a rise in inflation of more than 5% and sales of <edited> or <edited> have increased by 10% with respect to 2019.

In the **Netherlands**, some company and sector level agreements may include wage indexation clauses, known as “**general price compensation”** clauses. In 2021, it was estimated that approximately 26 collective agreements, mostly at the sectoral level, included such wage indexation systems. These agreements typically provide for a negotiated wage increase in addition to an adaptation to inflation on a regular basis. In some cases, the inflation adaptation is subject to a cap, and the collective agreements may also include hardship clauses.

The largest Dutch trade union confederation, FNV, is currently campaigning for the generalization of this system. In recent negotiations, FNV successfully included wage indexation clauses in sectoral agreements for painters and harbor workers. However, in some other sectors, such as the rail industry, the union was unable to secure automatic wage indexation, and instead agreed to a one-off inflation compensation.

Example from the Netherlands – wage indexation for painters

The wage increase for the period 1 January 2024 to 31 December 2024 shall be agreed by the parties to this CLA before or no later than 1 October 2023. The increase of the hourly wages in the wage scales (…) for the period 1 January 2024 to 31 December 2024 will be linked to the developments of the CBS consumer price index (…). In addition to this index, parties will consult with each other to assess whether the developments in the sector and the monitoring of the measures RVU and generation pact, as described in Article 63, paragraphs 3 and 4 respectively, give cause to implement an extra increase for the period 1 January 2024 to 31 December 2024

Example from the Netherlands – wage indexation in private security

2. In 2020-2023, wages increase by at least 2.5%

a. Or by the percentage of the Consumer Price Index (CPI) if it is higher than 2.5%.

b. For this, your employer looks at the average CPI for the months of October to September of the previous year.

Example from Turkey - wage indexation clause in media sector

(…) These amounts are increased in the second year of the contract at the rate of the increase in the Consumer Prices Index with 2003=100 Base Year of the Turkish Statistical Institute's 2023/February index number (compared to the same month of the previous year) compared to the 2022/February index number (compared to the same month of the previous year).

2.3 Automatic renegotiation – Italy

It's worth noting that in some countries, there are lighter versions of automatic wage indexation systems, such as automatic renegotiation when inflation crosses a certain threshold. This type of system is found in some Italian collective agreements, where a "**verification clause**" in a new collective agreement in the insurance sector allows for yearly re-evaluation of wage elements in light of inflation.

In other cases, such as in older banking collective agreements, there is a clause that corrects previously underestimated inflation with a wage adaptation, but with a time lag. While these lighter versions of automatic wage indexation systems may not provide the same level of certainty as full indexation, they can still help protect workers' purchasing power in the face of inflation.

Example from Italy – wage revision in the Italian insurance sector

Quite exceptionally, the Parties agree that if price trends should be characterized by extraordinary increases in inflation, measured with the index "HICP excluding imported energy" and the labor market should experience heavy negative repercussions linked to the economic crisis deriving from the complex international political framework, the Parties will be able to take steps to verify the consistency between the inflation forecast to define the contractual increases recognized at the time of renewal and the inflation actually observed. they will meet by 31.12.2023 for an overall assessment of any critical issues.

2.4 No systems of wage indexation

In a number of other countries, there are **no** automatic or semi-automatic wage indexations. All collectively agreed wage increases or adaptation are the result of negotiations based on a number of indicators, of which rising living costs is one. This is the case in Switzerland, Germany, Denmark, Sweden, Finland, Norway, and the United Kingdom. In France, while there is an official prohibition against including automatic wage indexation systems in collective agreements, some agreements link the lowest wage scales to the minimum wage, which is regularly adjusted for inflation.

3 Conclusion

While automatic wage indexation systems in collective agreements were not a major topic during the past few decades of low inflation, since the recent rise in inflation in 2021-2022interest has risen remarkably. In certain scenarios, these systems guarantee wage stability in real terms, but at the same time, they might limit room for wage increases in negotiations.

An overview of existing practices collected by UNI Europa reveals the following key points:

- There is a wide range of mechanisms through which collective agreements attempt to link wages to inflation trends to avoid unexpected losses in purchasing power.

- Since the increase in inflation, the number of experiments and innovative collective bargaining solutions has expanded, with unions in some countries attempting to make these systems more widespread across all collective agreements.

- While in many EU countries unions are attempting to broaden the use of automatic wage indexation systems, the practice is largely absent in a number of countries. This is due to trade union tradition or strength in some countries and trade union strategic choices in others.

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For any comments, questions and remarks, please contact the author: Stan De Spiegelaere – stan.despiegelaere@uniglobalunion.org

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