

Background

Please confirm you have read and understood this important background information.

Yes, I have read and understood the information on this page.

About you

1 What is your name?

Name:

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Organisation:

Section one: Measuring prices across the economy

1 Should ONS identify a main measure of price change across the economy?

Yes

Why? Please provide comments.:

Note: I am assuming this question refers to consumer prices.

Most countries have a "main" measure of consumer price inflation. In the EU, all countries are obliged to produce the HICP, and most produce a "national" CPI, which is generally treated as the "main" index in terms of publicity and used for a variety of uprating purposes. National statistical offices (NSIs) cannot of course force users to use a particular price index. That choice is up to the user. What an NSI can do is to provide guidance and advice as to which particular price index is best suited to the various potential uses. (The ONS needs to do more in this matter). In my view, two classes of consumer price index need to be produced. One is an index which is often referred to as a "macroeconomic" index; such an index is compiled with a view to providing governments and other agencies such as central banks with an index which adheres to conventional macroeconomic standards. For example, interest payments are excluded; taxes related to income or wealth are excluded; owner-occupied housing costs are measured by reference to actual rents; coverage is based on expenditures both by residents and foreign visitors; the so-called "plutocratic" (i.e. expenditure-weighted) approach is used. The UK CPI – which is of course the European HICP under another name – is just such a macroeconomic index. As the statistician responsible at Eurostat for developing the HICP from 1991-2002 I am in a good position to say unequivocally that the HICP was designed with very specific macroeconomic purposes in mind. These were twofold. Firstly, it is necessary to be able to compare EU national inflation indices using harmonised methods of compilation, so that it becomes possible to determine which countries pass the inflation-rate criterion for euro area membership. Secondly, the national harmonised indices can then be combined to form an aggregate index for the euro area. This was - and is – used by the European Central Bank as a main tool for setting the euro area interest rate. These original purposes still stand today, and will no doubt continue to do so for the foreseeable future.

The other type of consumer price index which must be produced is often referred to as a "household-based" index, i.e. measuring inflation as it affects households. Indeed, this is cited as the principal use of a CPI by the international Consumer Price Index Manual. The RPI served for almost half a century as the UK's main inflation index. It may have had its faults (which index doesn't?) but it was accepted by the majority of the public as the definitive rate of inflation. That is because it was essentially a measure of inflation "as perceived and experienced by consumers" - to quote the above-mentioned international Manual. Three particular attributes may be mentioned. One is the inclusion of mortgage interest as a measure of owner-occupiers' housing expenses. A second is the inclusion of Council Tax. A third is the use of an overall weighting scheme which approximates to a so-called "democratic" approach – weighting by households, rather than the so-called "plutocratic" approach referred to above. Today, the UK is in the regrettable situation in which the RPI is no longer designated as a "national statistic" (even though it is widely used, including by the government and other public sector organisations). And the only other "main" index published by ONS is the CPI, which is not designed for the same purposes as was the RPI. Assuming that the RPI, for political and legal reasons, cannot be resurrected as a main index, we are left with a serious gap in UK inflation indices, a gap which can only be filled with a new household-based index such as the HII (see 2a below). The HII should be presented as the main index for household inflation. It is not right for the public to have to make a choice among two or more inflation indices, or to suffer the present confusion of having incomes and prices uprated by two different indices. It undermines the credibility of all the published measures of inflation.

2 If you answered 'yes' to question 1a, then what should this measure be?

Other (please provide details).

Why? Please provide comments.:

As my answer to Q1 makes clear, there is no existing index which is capable of acting as a main household-oriented index. A new index must therefore be

created. As a member of the Paul Johnson panel of advisers, I prepared a short paper in early 2014 (“Options for a new Household Inflation Index”) which was referenced in the Johnson Report. In 2015, the Royal Statistical Society asked Jill Leyland and myself to write a fuller paper based both on my 2014 paper and a paper by Leyland (“What should an uprating index look like?”, 2014) which addresses the same issues. The new paper is available on the Statistics Users Network website.

The index we have proposed has been given the working title of Household Inflation Index. This is not the place to rehearse all the arguments given in the paper; I hope it will be carefully studied by those reading this submission. I am convinced that its essential features could and should form the basis of a new household-oriented consumer price index, replacing the RPI and being an essential complement to the CPI.

The Johnson report proposed that CPIH should become the main UK inflation indicator. I disagree fundamentally with this proposal for several reasons. Firstly, as discussed in 1a above, CPIH is a macroeconomic index, unsuited to measuring household inflation.

Secondly, CPIH is essentially the HICP, with OOH costs, proxied by rental equivalence, tacked on. The latter measure is required in order to produce an index appropriate for national accounts deflation purposes (as OOH costs are also proxied by equivalent rents). The point has been frequently made that the rental market usually behaves very differently from the OOH market and is therefore unsuitable as a proxy measure. Moreover, the concept of rental equivalence is alien to the perceptions of most individuals. For an owner-occupier to have, say, his or her state pension linked to movements in rents (which have a weight of over 20% in the CPIH) would be unacceptable – and rightly so.

Thirdly – assuming that CPIH eventually regains its “national statistic” status – it would need to be re-launched under a new name. The name “CPIH”, with the “H” standing for “Housing”, is patently unsuitable for a major national index, while acceptable as a technical index for specialist users – as with RPIX.

Fourthly, the EU is planning to introduce OOH costs into the HICP – and hence the UK CPI – within the next few years, using the “net acquisitions” approach. One can imagine nothing more confusing to the general public than having CPIH (with rental equivalence) published by ONS alongside the CPI/HICP (using net acquisitions) and RPI (using mortgage interest and depreciation). A new Household Inflation Index acting as the main inflation indicator would rapidly make RPI redundant (apart from its role in index-linked bonds), leaving CPIH to remain as a technical index for specialist use. The CPI, of course, should still be published as the main macroeconomic index, as used by the Bank of England for setting the interest rate and for making international comparisons of inflation, as well as other technical uses.

The CPI itself, as a macroeconomic index, is not a suitable index for general use, particularly for uprating incomes or prices, and is in any case beyond the control of ONS as it must comply with all of the EU Regulations for the HICP. In addition, it has recently come to light (Flower and Wales, ONS, 2014) that the implicit expenditure profile of the CPI corresponds to that of consumers in the upper deciles of the expenditure and income distributions. This cannot be acceptable to the general public. The main price index must be one which is acceptable to the public at large; without such acceptability it is unlikely to achieve wide usage – and nor should it.

3. Should its production be governed by legislation?

No

Why? Please provide comments.:

I do not think it is sensible to have an index as important as a main index of inflation to be constrained by legislation which will inevitably become increasingly divorced from the changes which the passage of time will surely necessitate. The overall price index governance arrangements should ensure that what is required will be achieved.

Section two: Measuring consumer price inflation for different household types

4 Should ONS seek to measure changes in prices as experienced by different households?

Yes

Why? How often? Please provide comments.:

As the Astin/Leyland (2015) paper makes clear, the HII would be well placed to become the head of a family of subsidiary indices, relating to different household types, household income levels, regional differences and so on. The exact choice of such subsidiary indices would be left to the producers, guided as necessary by UKSA and the Advisory Panels on consumer prices

The Johnson Report also recommends such subsidiary indices, though only at an annual frequency. I see no good reason to restrict such indices to an annual publication, provided the costs of monthly publication are not prohibitive.

5 If yes, how should ONS seek to do so?

Using a payments-based approach.

Why? Please provide comments.:

To say I prefer a “payments-based approach” is to simplify a very complex issue. An HII or similar would seek to measure the impact of inflation on household budgets. To this extent it should relate to payments actually made, approximately at the time they are paid. The more important of these two factors is the definition of “payments actually made”. As the Astin/Leyland (2015) paper argues, this implies that an HII should include the full amount of loan interest for the purchase of goods and services, regardless of the type of product. It would therefore include mortgage interest on house purchase, interest on student loans, interest on loans for the purchase of cars and other durables etc. It would also cover Council Tax, which is a tax closely related to the occupation of dwellings, and not related to income or expenditure.

A secondary issue concerns timing. In the majority of transactions “acquisition” and “payment” are simultaneous – ignoring any small differences such as the timing of payment of purchases made using credit or debit cards. In cases where payments are spread over long periods of time, such as mortgage interest or student loan repayments, regard must be had to the timing of payment, since this has an important impact on households’ budgets.

Section three: The RPI

6 Do you use the following indices? (Please select those that you use)

If yes, for what purposes? Please provide comments.:

I am not a “user” of any of the above indices. Indeed I am not a “user” of any price index, except to the extent that I need to have a deflator of my own personal expenditure and income so that I can calculate in approximate “real” terms the extent to which my expenditure and income are rising or falling. For this, I need an index which covers my household outgoings, and this is closer to the RPI or RPIJ than the CPI or CPIH. An HII would be even better.

7 Do you agree that the following indices should be discontinued? (Please select those that you suggest should be discontinued)

Why? Please provide comments.:

I think that as long as the RPI has to be produced, there would be no need for any of the above indices to be produced, provided that a suitable household-based index, and a variety of subsidiary indices, is published.

8 Do you have any views on what 'freezing' changes to the RPI should mean in practice?

Yes

Why? Please provide comments.:

I do not think that freezing the RPI is sustainable in the long term. I realise that there are legal requirements to continue to produce the RPI, using largely unchanged methodologies, for the holders of index-linked bonds. But this index should be published only in the relevant technical publications and not offered as an alternative to the main indices, CPI and, hopefully, HII.

Meanwhile, the government and other public bodies should as soon as possible make a transition from using the RPI – which is no longer a “national statistic” - as an uprating index for incomes and prices to a more suitable index, such as an HII should be. Logically, there seems no reason why the same index should not be used for uprating both household incomes such as state benefits and regulated prices.

Section four: Evolving consumer price statistics

9 Are the priorities identified by ONS in its forward work plan appropriate?

Not Answered

Why? Please provide comments.:

I think a top priority is the rapid development of a monthly Household Inflation Index. This could be followed by a family of mainly monthly subsidiary indices as resources permit.

Of the other issues referred to in the consultation document, I would place higher priorities on:

- EU Compliance – this concerns the CPI, together with OOH and HPI indices;
- Location Boundary Review – particularly if regional price indices are to be produced;
- Alternative sources – this should be a permanent priority, as data sources such as web-scraping become potentially available;
- Transparency and processes; there is much room for improvement here;

In addition, I would suggest devoting more resources to improving and monitoring methods of Quality Adjustment.

10 Should ONS include council tax in the CPIH?

Not Answered

Why? Please provide comments.:

Given my view (see Q2) that CPIH is not a suitable index for general use, I have no view on the whether or not Council Tax should be included in it. The decision should be made after consulting the technical users of CPIH.

Additional information

Do you have any further comments relevant to this consultation?

Do you have any further comments relevant to this consultation?:

I hope that the actions resulting from this important consultation will not be influenced by any form of governmental pressure on UKSA or ONS.

User satisfaction

Overall, how satisfied were you with this online consultation service today?

Satisfied

Please tell us if there are any specific areas for improvement, or if you have any other comments.:

In several instances, a requirement for a straight "Yes" or "No" answer is unrealistic.