

# Template for response

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The Authority encourages respondents, where possible, to provide their submissions [online](#).

Where you would prefer to respond via email or on paper, please use this template and return the submission via email to [cpi@ons.gsi.gov.uk](mailto:cpi@ons.gsi.gov.uk), or via post to:

*Consumer Prices Consultation team  
Government Buildings  
Cardiff Road  
Newport  
South Wales  
NP10 8XG.*

I support the views expressed in the response to the consultation submitted by Tony Cox on behalf of the RPI/CPI user group.

I have two further points related to **question 9a** of the questionnaire where ONS advised that comments that do not fit naturally within with the questionnaire should be added. They both relate in part to the issue of non-comparable substitutions or implied quality change.

**Point one expands upon the RPI/CPI user group response to question 9a about ONS resources.** There is a great deal of analysis and research that is needed and it will stretch ONS resources so there is a need to look outside the organization for additional resources to enable important research and analysis to be carried out in parallel.

The issues surrounding price indices are nationally very important and there is basic research that needs to be done. This would suggest that the research councils are a possible source of extra resources and could be approached to see if it would fall within their remit to offer help.

There are, of course areas of work – for example, on the formula effect – where a significant amount of work has already been carried out by ONS and it would make little sense to move much of that work elsewhere. However, there appears to have been little research or analysis done on implied quality change either in ONS or elsewhere. This makes it an area in need of basic research in a number of disciplines potentially including economics, sociology, mathematics and statistics. I have suggested the potential to use a Bayesian approach but there are other possible approaches related, for example, to PPP comparisons across economically diverse countries.

**Point two is not included in the RPI/CPI user group response and relates to the priority cited first in the work plan that both the CPI and CPIH are produced “to the best possible standard, as recommended by Mr Johnson in his review”, and more importantly to quality issues with the use of RE within CPIH**

The “best possible standard” priority is cited first in the ONS work plan. It is a strange objective for statistics which would normally be produced to a standard defined by what is sufficient to meet the user requirements. This more normal approach would balance cost, accuracy and precision in line with the code of practice. Clearly the HICP needs to be produced to meet European regulations though there would appear to be little reason to go beyond what is strictly necessary for that purpose. Under present regulations and arrangements CPI and CPIH (excluding its OOH component) would therefore meet the standards of the HICP.

However, CPIH is likely to diverge from the HICP when an OOH component is included in the index because HICP is unlikely to use RE as the OOH component. CPIH is therefore likely over time to be superseded by the HICP with its OOH component. There seems little point in putting any substantial work into CPIH beyond keeping it in line with the non-OOH part of HICP.

In addition to the likely longer term issues associated with the RE OOH component of CPIH, there are immediate quality issues with the index. These issues are related to non-comparable substitution and implied quality change.

The quality issues with the use of the RE index in CPIH are briefly outlined below.

I plan to submit a more detailed analysis to the UKSA monitoring and assessment team as part of the reassessment of the national statistics status of CPIH.

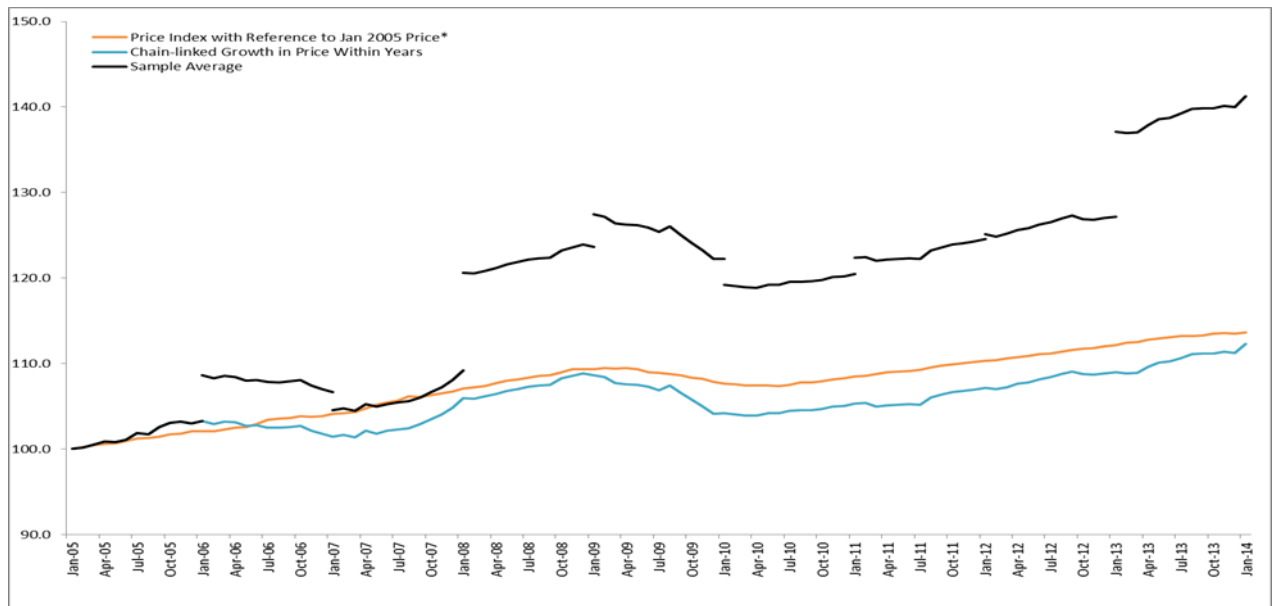
The analysis ONS published in January to support the reassessment for National Statistics suggests that the revised series for RE developed by ONS has created, exacerbated or simply revealed a larger potential problem.

There are three broad issues. These are –

- The scale of the non-comparable substitutions/implied quality change in the RE index.
- The large weight (slightly over one fifth) of CPIH attributed to the RE index when both the rental and the impute OOH components are added together.
- The limited control and access ONS have over the RE data.

The scale of the implied quality change in the RE index can be seen in the following chart provided by ONS.

Rental Equivalence – implicit within-year and between-year quality changes, 2005-2014



This chart was not included in the ONS paper “Improvements to the measurement of owner occupiers’ housing costs and private housing rental prices” published on 31<sup>st</sup> January 2015. ONS have recently indicated that they have carried out no further work in this area.

The chart shows the increase in observed rents between January 2005 and January 2014 is about 41% compared to about 14% for the RE Jevons index. This gives a difference of about 27 percentage points between the two. The total weight within CPIH for RE taking into account both rents and OOH is slightly more than 20%. This implies an upper bound of about a 5 percentage point increase in CPIH available from RE for a different approach to estimating implied quality change and sellers’ margins. In practice any increase in the CPIH from increased sellers’ margins would be less than 5 percentage points. However, unless sellers’ margins accounted for less than 4% of the total change they would represent a larger change in the index than resulted from, for example, the recent revision of 0.2 to the published CPIH index in 2015.

In addition to the sellers’ margin issue, the 20% weight of the RE index in the CPIH implies that it requires to be of a particularly, possibly unreasonably, high quality. If such a high quality is not achievable then because of the large weight errors, biases etc in the RE index are likely to be reflected through into CPIH. ONS has limited access to VOA data which will make it difficult for ONS to reliably ensure the high quality required of the RE component of CPIH.

To conclude the case has not been made by ONS for prioritizing work on CPI and CPIH beyond what is strictly required to meet regulations relating to HICP.