

# **Response to UK Statistics Authority Consultation Paper**

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## **Measuring Consumer Prices: the options for change**

The RPI CPI User Group operates under the auspices of the Royal Statistical Society, but is independent of that organisation. It comprises approximately 160 members and hosts both public face to face meetings and discussions on line via the Statistics User Net web-site.

The User Group response to this consultation is the result of an initial meeting (open to all) in mid July, comments on SUN, an initial draft posted on SUN, 13 August, further comments (both on SUN and by email), a second meeting open to all on 4 September with a number of participants which went through the draft response section by section. Finally the result of that meeting was posted to SUN on 9 September for any last minute comments. The aim throughout has been to produce a comprehensive and fair consensus of the views of the User Group. Of course, not all members of the User Group will endorse everything our response says and in addition to the above process we have encouraged User Group members to make their own individual responses to the consultation which represent a further rich source of ideas for the UKSA to call upon.

## **Section One: Measuring prices across the economy**

**4. Should ONS identify a main measure of price change across the economy?**

- a. Yes
- b. No

**1a. Why? Please provide any comments below:**

*The primary purpose of, “a main measure of price change across the economy” should be to inform the public in a way that reflects their experience of changing prices and that they can understand. This necessitates a single headline measure of inflation, but cannot be achieved with the current consumer price indices which reflect technical macroeconomic models of the economy.*

*The CPI is the UK version of the HICP which is produced in accordance with EU Regulations. It was designed to compare inflation rates across Europe, but to achieve agreement across Europe compromises were necessary and in particular it does not yet include OOH costs. It remains suitable for the purpose for which it was designed, but does not qualify as a “main measure of price change across the economy” and the UK now uses it for purposes for which it was not designed. Very few European countries use the HICP as their main measure of inflation.*

*The CPIH is an attempt to correct the omission of OOH costs. However, instead of measuring these costs directly it uses a proxy measure of rental equivalence. Adopting a proxy for such a significant element (circa 20%) of a UK price index is reason enough to regard CPIH as unsuitable as a “main measure of price change across the economy” that the public can understand as reflecting their experience.*

*The RPI CPI User Group has proposed that a Household Inflation Index (HII) should be developed to measure the change in prices as experienced by UK households. This would then become the main measure of price change for the UK, retaining the CPI and CPIH as technical indices designed for macro-economic purposes.*

*Of currently available indices the RPI remains the most suitable measure of household inflation for many reasons, including its targeting of UK household expenditure and inclusion of OOH costs. However, the User Group considers this could be improved upon significantly by developing a HII.*

*RPIJ shares most of the characteristics of the RPI and hence similar arguments apply. However, the rationale for RPIJ is of concern, especially as the ONS has not engaged in a detailed debate about the evidence for the suitability of different formulae for particular circumstances*

*Both the CPI and CPIH are expenditure weighted indices which is another major factor that makes them unsuitable as indices that measure price changes experienced by UK households. ONS research has shown that the CPI most accurately represents CPI measured changes in prices for the 7<sup>th</sup> expenditure decile. The user group does not regard it as desirable for the headline inflation measure to reflect the expenditure of the more affluent in society and should target the typical (modal) household.*

If yes:

**2. What should this measure be?**

- a. ~~the CPIH, as recommended in the Johnson review. The CPIH includes owner-occupiers' housing costs. It does not currently hold the *National Statistics* designation (although its re-assessment is due to commence shortly). The index is a UK measure, designed by ONS to meet UK needs.~~
- b. ~~the CPI, ONS's current headline measure. The CPI is an EU measure, designed by Eurostat to ensure comparable consumer prices statistics across the EU.~~
- c. other (please provide details).

**2a. Why? Please provide any comments below:**

*A Household Inflation Index would fill a significant gap in the current range of UK price indices and provide the main measure of price change across the economy as experienced by UK households. It would better reflect the inflation experience of the typical (modal) household, include a more realistic interpretation of housing costs and better coverage of people's spending behaviour.*

*CPI and CPIH are technical indices most appropriate for use in National Accounts calculations, suitable for experts who have sophisticated ways to access ONS prices data and will not be disadvantaged if their preferred indices are not regarded as a main index.*

**3. Should its production be governed by legislation?**

- a. ~~Yes~~
- b. No

**3a. Why? Please provide any comments below:**

*The rationale for saying no to governing the production of a HII in legislation is that the User Group regards parliamentary legislation as a cumbersome method of regulating a price index at the detailed level.*

*However, it is important that the production of such an index should be governed by a strong and robust independent governance structure. It is also important that such an index is guaranteed to continue to be produced for the foreseeable future. These principles of production could be appropriately enshrined in parliamentary legislation.*

*In the case of the RPI it can be argued that the Bank of England performs the role of an independent adjudicator in cases when a major change of the index is proposed. In the case of the CPI any changes in the index construction are laid down in EU Regulations.*

*It is unlikely that either of these options would be appropriate for a HII and so a new structure would need to be devised.*

## Section Two: Measuring consumer price inflation for different household types

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

- i. Yes
- ii. No

#### 4a. Why? How often? Please provide any comments below:

*As explained in our answer to Q1, the UK lacks an index designed to measure the change in prices as experienced by households. The priority must therefore be to urgently address this omission. The User Group has proposed that such an index should be produced and has termed it a Household Inflation Index. (An example of a proposal for such an index has been made in the Astin/Leyland paper published in May 2015 and available in the [library](#) of the RPI CPI User Group web-site)*

*Once such an index is established, or in parallel with its development, consideration should be given to the needs of measuring changes in prices as experienced by different households.*

*A family of HII indices could consist of households divided by socio-economic group (income band), geography (region) or other characteristics (e.g. age groups). These would all be subsidiary indices, useful for research and potentially for policy decisions, but should not detract from the priority of producing a UK wide Household Inflation Index.*

*The main HII should be produced on a monthly basis in line with other major statistics. In principle the complete family of HII indices should also be produced on a monthly basis, but this could be modified, depending on demand, if there are significant cost savings to be made from producing the subsidiary indices on a less frequent basis, or by delaying their publication until later in the month.*



If yes:

**5. How should ONS seek to do so?**

- i. Using a payments-based approach.
- ii. ~~On the same basis as existing measures such as CPI.~~
- iii. ~~Via another means (please provide details)~~

**5a. Why? Please provide any comments below:**

*A payments based approach should be the target approach as this accords most directly with households' experience of price changes. However, there is a legitimate debate between an acquisition and a payment approach for certain items and there may be practical reasons for using an acquisition approach where this does not materially alter the result .*

*The principle should be to recognise the full price of an item plus interest payments on loans, as these are the payments made by the household.*

*Examples of where there may be a material difference between the two methods are payments for the purchase of education, houses, cars, holidays. In each of these cases the payments may, in whole or in part, differ from the time of "acquisition". For example, student fees are incurred at the point of 'acquiring' a university education, but are often re-paid after acquisition and over a period that may extend to decades. Furthermore, the total cost may be significantly increased by the interest that then becomes due. A further consideration is that a proportion of loans may not be re-paid in full or in part. The cost to the household is the actual payments made and it is these that should be reflected in a HII.*

## Section Three: The RPI

### 6. Do you use the following indices?

i. RPIJ<sup>1</sup> Yes/No

ii. Tax and price Index Yes/No

iii. RPIY<sup>2</sup> Yes/No

iv. RPI pensioner indices Yes/No

v. Component indices of the RPI Yes/No

vi. Any other RPI analytical- or sub- index Yes/No

### 6a. If yes, for what purposes? Please provide any comments below:

*Of the existing indices within the RPI family the User Group attends in the main to the RPI itself. However, we understand that the derivative indices listed here are used to gain greater understanding of changing prices and for research purposes. For example, component indices of the RPI can be used to throw light on the most significant drivers of overall price changes at different points in time.*

<sup>1</sup>

RPI calculated using formulae that meet international standards

<sup>2</sup>

RPI excluding Mortgage Interest Payments and indirect taxes



**7. Do you agree that the below indices should be discontinued?**

i. RPIJ	Yes/No
ii. Tax and price Index	Yes/No
iii. RPIY	Yes/No
iv. RPI pensioner indices	Yes/No
v. Component indices of the RPI	Yes/No
vi. Any other RPI analytical- or sub-index	Yes/No

**7a. If yes, why? Please provide any comments below:**

*We do not have a strong view on maintaining the RPI family of indices, apart from the RPI itself, currently produced by the ONS. However, as the RPI must continue to be produced it would appear to require only a very modest effort to keep the whole family of RPI based indices. We therefore propose that they are kept unless the ONS can explain why that would present difficulties or be unduly expensive.*

*Once a HII is established the RPI sub-indices could be replaced by HII sub-indices.*

**8. Do you have any views on what 'freezing' changes to the RPI should mean in practice? Please provide comments.**

*It is difficult to understand how the ONS can remain credible if it continues to produce a statistic that is not updated in line with best practice but is claimed to be produced to the highest standards. The RPI should therefore not be 'frozen', but should continue to be improved in line with good practice.*

*In reality it is accepted that the RPI will remain in use for the foreseeable future. The UK Pension Protection Fund in its, "Long Term Funding Strategy Update" paper published on 27 July 2015 has accepted that the long-awaited market for instruments linked to the consumer prices index (CPI) is unlikely to materialise and that such instruments will remain linked to the RPI.*

*This and the government's continued use of RPI for various purposes strengthens the case to ensure that the RPI is not frozen, but continues to be improved.*

*The sort of changes that should continue to be made to the RPI are those that have been made over the last half century. These changes responded to changes in spending patterns within society. The ONS should seek and receive advice from its advisory groups (expected to be established at the end of this year) on changes that should be made in the future.*

## Section Four: Evolving Consumer Price Statistics

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

- a. ~~Yes~~
- b. No

#### 9a. Why? Please provide your comments below:

*The main priority should be to develop a HII. Although the work-plan refers to measuring inflation as experienced by different households it is not clear if this involves developing a purpose designed measure of price change as experienced by households. In the User Group view this is essential.*

*The User Group has identified the following priorities for the ONS-*

- 1. To develop a Household Inflation Index*
- 2. A thorough analysis of data collection methods and the most appropriate formula to be used at the first level of aggregation for items when direct information on weights is unavailable should be continued, building on recent research by the ONS.*
- 3. To conduct research into product item definitions, non-comparable substitutions, or implied quality change, and their effects in both the short and the long term including issues such as changes in product reliability and the rebuilding of sellers' margins.*
- 4. Once a Household Inflation Index is established, or in parallel with its development, consideration should be given to the needs of measuring changes in prices as experienced by different households and by households in different regions.*
- 5. Establish an effective governance system that is transparent about changes to the index and ensures regular and thorough reports that investigate additional or alternative sources that provide more comprehensive and accurate price quotes.*
- 6. The ONS should consider whether additional external resources, e.g. via the research councils, could assist in taking forward some of its work if its own resources are not always sufficient.*
- 7. Work on 'superlative indices' and COLI should not be considered a priority. These are matters of academic interest and should not be accorded high priority.*

**10. Should ONS include council tax in the CPIH?**

- a. Yes
- b. No

**10a. Why? Please provide your comments below:**

*The User Group does not take a position on this question.*

*Council tax is not a tax based on income and should not therefore be omitted from a price index. However CPIH as currently devised has the serious shortcoming of using the proxy of 'rents' to represent Owner Occupied Housing (OOH) costs. This make the CPIH an unsatisfactory index for most purposes and adding a council tax item to it will not alter that.*

*For 'macro-economic' purposes the CPIH is likely to be superseded by a new European index that will include accounting for OOH costs using a net acquisitions approach. Neither the CPI nor the CPIH are suitable as a measure of the changes in prices affecting households. It is therefore unclear what role the CPIH should have within the family of indices produced by ONS.*