Next steps for Household Costs Indices

Jill Leyland (with input from Chris Payne and Abi Casey)

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Last July we had a hurried discussion on next steps for Household Costs Indices but there was not sufficient time to consider the issues in full or to enable any real assessment of priorities.

HCIs are now published quarterly. Data are currently available up to the end of March 2023 covering the bulk of the cost of living crisis and demonstrating that inflation experienced by most households during the crisis, particularly those on lower incomes, was noticeably higher than that shown by CPI or CPIH. It is also clear that a number of people and organisations are already slowly starting to use HCIs or pay attention to them. The ONS budget is currently heavily constrained, and likely to remain so, so it is therefore important that priorities are clearly established so that whatever money is available is spent most effectively.

Practically all the developments initially planned by ONS have been incorporated. So a key point to consider is when to apply for Accredited (National Statistics) status. Given the changes to RPI in 2030 it would seem logical to aim for this to happen by 2028 so that users who prefer, and are able, to switch from RPI to an HCI rather than remain on RPI transformed into CPIH (as foreseen in the original RPI proposals put forward by John Pullinger in 2017) have properly accredited series to consider. ONS advises that two years needs to be allowed for the accreditation process to cover both the assessment itself and the incorporation of any required changes. This therefore leaves only limited time for changes before making the application. (Note that the original plan was to obtain national statistics status by the middle of this decade.)

A number of additional developments have at times been discussed by the panel. There is a trade-off between how many can or should be incorporated prior to seeking accredited status and when the application is made. It should be noted that accreditation does not end development; indeed, the Code of Practice makes it clear that all accredited statistics have to be open to improvement.

Question: Does the panel agree with 2028 as a target for accredited (national statistics) status?

This paper aims to list all possible developments/improvements that have been suggested so that panel members can consider them at the July meeting. This would include, in particular, deciding what is essential before accredited/national statistics status is granted and what can be left until after. Further background information and explanation on many of these points can be seen in the Paper "Measuring Inflation as Households see it " by John Astin and Jill Leyland.

To give a guide to resources needed, ONS has provided an idea of time needed for each point in terms of one full time equivalent member of staff. In the below, ST = 3-6 months; MT = 6 months to a year; LT = 1 year upwards.

In addition to points which arise from the "Measuring Inflation" paper, ONS would like to highlight the following background work which is either desirable or essential:

a. Further system and process improvements could still be made to shore up quality assurance of the data, and bring the processes and checks into line with the standard expected for a national statistic measure. A lot of this is behind the scenes stuff but, as an example, improvements to the system functionality would, as a by-product, allow ONS to readily deliver on point 7 below. (MT)

b. There are a number of areas where the input data sources could be improved, for example some of the interest expenditure variables or some possible small changes to the Living Costs and Food Survey (LCFS) which provides the bulk of the weights used. These issues are not particularly visible at the moment, but the assessment process is expected to include a review of this. (ST to MT)

The order in which the following points are listed is not intended to imply any relative importance.

1. Filling in gaps. I am aware that interest on "pay day loans" and similar are not included. Are they still important? I understand that the Financial Conduct Authority collects data. A wider range of payments plans for student loans could also be incorporated. Related to this ONS suggests a review of payments methodologies to assess consistency on HCI-specific items could also be carried out. ST to MT depending on number of gaps.
2. Change from residential to national statistics basis. We are unsure of the practical importance of this. The Dutch Statistics Office provided some information on the impact of including expenditure abroad (see appendix). MT
3. Putting items where there can be a long gap between payment and acquisition (eg theatre tickets, package holidays) on a payment rather than an acquisition basis. ST (to MT)
4. Further consideration of methodology for mortgage interest. A change to the methodology used by mortgage lenders has been considered. We asked in an earlier meeting for some limited further investigation. Changing to it would correct the exaggerated movements around the time of the financial crisis. It also enables mortgage capital payments to be estimated (see below). An alternative would be to keep the RPI methodology but use the average effective rate back before 2010. (Prior to 2010 the RPI used the "standard variable rate" which is highly sensitive to changes in bank rate. This creates an exaggerated

movement around the time of the financial crisis since in practice most households were on short-term fixed rates at that time.) MT

5. Research into how different choice of products by different household groups affects relative inflation and whether HCIs should be adapted for this. In particular, do low-income households, who predominantly buy value/own brand products, experience different inflation to other income groups? The panel has always attached importance to this.
   ONS commissioned work by Strathclyde University (Fraser of Allandale Institute) which was presented to panel members on April 27th. They focused on goods, leaving services to a later date, and suggested four possible approaches:
   a) Purchase commercial household scanner data
   b) Link supermarket scanner data to household characteristics via store membership cards, information about consumer's or store's postcode etc
   c) Update the LCFS collection methodology to get more specific information on goods purchased, quantities, and average unit prices
   d) Use a periodic or one-off study to model dispersion in household group inflation rates relative to the all-household HCI rate, or household group adjustment factors for class-level price indices

   All of these would be complex so (very) long-term or potentially expensive or both. Would perhaps an interim measure looking at low-income households only be feasible in the shorter term? It is these households for whom this information is most needed since they will already be buying, largely, the cheapest items available so do not have the capacity to "trade down" that other households have. This could perhaps be a stand-alone series based on either an extension to the "least-cost" work that ONS did in early 2022 or, maybe, the research by Loughborough University (paper circulated earlier to panel members).

6. Capital elements of house purchase. "Measuring Inflation as Households see it" recommends that down payments for first time buyers and all mortgage capital payments should be included in HCIs or in a version of them (the paper sets out the arguments for this). (Down payments for second and subsequent buyers would not be included since these are normally at least partly, and usually substantially, funded by the sale of the existing dwelling.) John Pullinger, when National Statistician, recommended that a separate version of the HCIs including these and potentially other capital payments should be established once the current HCIs had reached national statistics status. LT (but note that if the Lenders' method were adopted at 4) capital mortgage payments would automatically be calculated).
7. Are there other household groups for which indices should be calculated? ST

8. Is the name “Household Costs Indices” the best option?
9. Are the indices using the right formulae? (Use of formulae is scheduled for discussion at our September meeting.) LT
10. Monthly publication with or without alignment with CPI/CPIH/RPI timetable, or alignment while retaining quarterly publication. LT

The following would probably be longer-term considerations, or indeed, not considered at all. They are included as reference and in case anyone feels they should have higher priority. There is more information in the Astin/Leyland paper.

11. Should pension contributions be included?
12. Should tax and NI payments be included? (Note: in the past HCIs have been compared to households’ disposable income.)
13. Should changes be made to the treatment of quality improvements where the “unimproved” product is no longer available for purchase?

Appendix 1

Expenditure abroad in the Dutch CPI

Expenditure abroad accounts for 4.05% of the Dutch CPI in 2024:

Food	Transport	Accommodation	Restaurants	Other
0.64%	0.94%	0.92%	0.93%	0.62%

Tourist expenditures abroad taken from national accounts (with adjustment for “just over the border” expenditures)

Compiled from other representative countries’ HICPs (with exchange rate adjustment for USA)

Index data are lagged by one month due to HICP publication schedules

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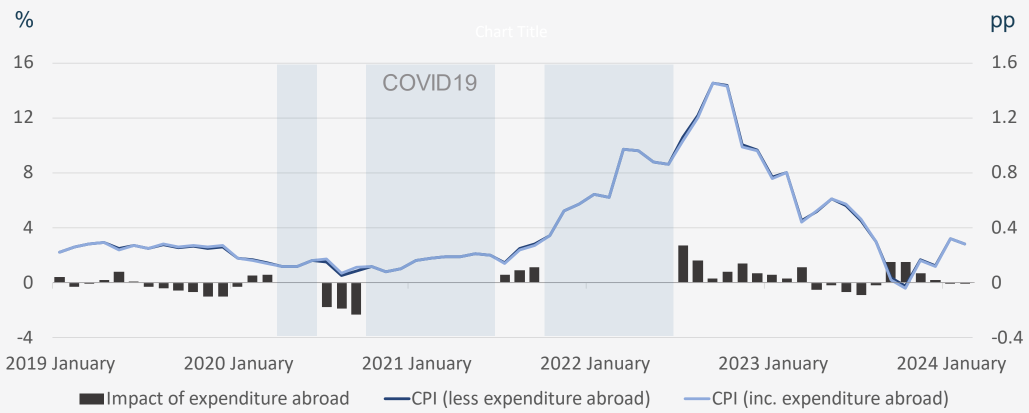
Impact of overseas expenditure on Dutch CPI



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