

14th November 2018

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Dear Chris and Rhys

This letter covers changes to consumer price inflation statistics in 2019. The letter addresses routine and non-routine changes to the suite of consumer price inflation statistics. This is provided for information.

## 1. RPI: NO PLANNED CHANGES AT THE TIME OF THE ANNUAL RE-WEIGHTING AND UPDATING OF THE BASKETS

### i. Issue

There are no planned changes to the coverage or basic calculation of the Retail Prices Index (RPI) proposed by the UK Statistics Authority (the Authority) for implementation alongside the update to the basket in 2019.

### ii. Action

To note the contents of this letter, which is being sent to acknowledge the requirements under Section 21 of the Statistics and Registration Service Act 2007. In previous years it has initiated the Authority's consultation with the Bank over whether any proposed changes to the RPI would constitute a fundamental change in the index which would be materially detrimental to the interests of holders of relevant index-linked gilts, and hence trigger the redemption clause.

### iii. Timing

For response by 4 January 2019.

## 2. RPI, CPIH, and CPI: Planned changes

Further to the information provided in the first section, which covered non-routine changes to the RPI, this section details other routine and non-routine changes to the suite of consumer price inflation statistics.

### 2.1. Routine changes to RPI, CPIH and CPI

#### *i. Mobile phone charges*

Once a year, the main mobile phone providers increase the price of existing customers' contracts by the RPI. In 2017 and 2018 three of the main providers applied the increase in April and one in May, using the published RPI rate of either December of the previous year or January or February of the current year. The existing mobile phone charges methodology does not generally reflect this additional cost to existing customers.

The current methodology<sup>1</sup> follows the cheapest package available from the main service providers for each of a set of customer profiles, based on voice, text and data usage. Company indices are further stratified by:

1. Pay as you go customers, who are free to switch packages following price changes
2. Monthly contract customers, who are usually locked into a package for 12 months or more; every 24<sup>th</sup> customer is assumed to have reached the end of their contract and thus switches to the cheapest package
3. SIM-only customers, who are usually locked into a package for 12 months; every 12<sup>th</sup> customer is assumed to have reached the end of their contract and thus switches to the cheapest package.

From the February 2019 index published on 20<sup>th</sup> March 2019 we intend to uprate monthly and SIM-only customer price indices in line with increases applied by mobile phone providers. The uprating will be applied in the month in which these changes take place, and will be applied in the same manner; that is, by RPI, or by RPI + X, for example.

If this change had been introduced in 2017 we would only have seen an impact on the headline RPI rate in two months between February 2017 and August 2018. These occurred in April 2017 when the headline rate would have increased by 0.1 percentage points from 3.5% to 3.6%, and in July 2018 when the headline rate would have increased from 3.2% to 3.3%.

#### *ii. Location Boundary Review*

In 2014 the sampling frame used to define the location boundaries for the suite of consumer price inflation statistics captured around 76% of total retail activity in the UK. New methodology has been developed to define the sampling frame which captures around 85% of the retail activity in the UK.

Following the live-pilot, which concluded in January 2018, all locations selected for replacement or re-enumeration will be drawn from the new sampling frame from January 2019. Around thirty locations are refreshed or re-enumerated annually, so we expect all locations to be on the new boundary basis by January 2022. Changes to the location boundaries will be carefully controlled to avoid overlaps with current locations within the sample.

It is considered that the introduction of a new sampling frame is a periodic routine change, necessary to maintain the suite of consumer price inflation statistics.

#### *iii. Annual Basket Update*

The annual update of the suite of consumer price inflation statistics will take effect with the February 2019 indices, which will be published on 20<sup>th</sup> March 2019. An accompanying article describing the changes to the baskets will be published on the ONS website about a week earlier. A fuller description of the reweighting and updating process can be found in the basket article for 2018, which is available online<sup>2</sup>.

The standard procedures for the annual updating of the baskets are well rehearsed. Although fixed within each year, the contents of the baskets of goods and services and their associated expenditure weights are updated annually to ensure they are representative of household spending patterns. The updating mitigates potential biases that might otherwise occur from not allowing for consumers switching purchases away from goods and services that have increased in price relative to those whose prices have reduced relative to other goods and services. Each year ONS conducts research into expenditure patterns to help inform decisions on which goods and services are under-represented and in which areas of the basket there is scope for removing items. Criteria

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<sup>1</sup> For a more detailed description of the current methodology please see section 8.4.5 of the [Consumer Price Indices Technical Manual](#)

<sup>2</sup> <https://www.ons.gov.uk/economy/inflationandpriceindices/articles/ukconsumerpriceinflationbasketofgoodsandservices/2018>

for choosing a set of items to represent particular categories of expenditure, such as clothing and footwear or food, include the size of expenditure and the diversity of the market based on information from the Living Costs and Food (LCF) survey, observed price variations based on historic data, and market research from a variety of sources on latest consumer trends. Information principally from the latest LCF and UK national accounts is used to update the expenditure weights.

It is considered that the changes in the contents of the Consumer Prices Index including owner occupiers' Housing costs (CPIH), CPI, and RPI baskets and the associated weights are not significant beyond their primary aim of ensuring the continuous and proper representation of consumer expenditure habits.

#### *iv. Transformation of inflation statistics*

ONS is improving its systems for producing above item aggregation and chain linking for RPI, CPIH and CPI by moving these onto our strategic Oracle supported platform (CORD). The new system is a fully supported application and provides additional visualisation tools that will make data analysis easier for our production teams. The expectation would be there is lesser scope for error as we move to common, corporate platforms. The new system will not revise historical data and there will be an extensive period of business acceptance testing and parallel run before it is used in production in April 2019.

Elementary aggregation functions will remain on existing platforms until a strategic platform has been developed.

## **2.2. Changes that only affect CPIH and CPI (non-routine)**

### *i. Double price updating at COICOP5*

In the February 2017 index, we introduced an additional level of aggregation (COICOP5) alongside a double price update of the weights: once in January to reference December prices, and again for February to December to reference January prices. This improvement makes the CPIH and CPI double chain link mathematically identical to a single chain linked index<sup>3</sup>.

Currently the double price update is applied at the COICOP4 level and above. From the February 2019 index, published on 20<sup>th</sup> March 2019, we are planning to also apply this double price update at the COICOP5 level. Our analysis suggests that the impact of this change would not be significant at any level of CPIH and CPI.

## **3. Designation of the UK House Price Index as a National Statistic**

We are pleased to inform you that on 18 September 2018 the Office for Statistics Regulation designated the UK House Price Index as a National Statistic. The UK HPI is used in the calculation of the housing components of the RPI. A letter from the Director General for Regulation details the actions that were taken to meet the requirements as set out in the UK HPI assessment report.

Please let me know if you have any queries or would like to discuss any of the changes raised in this letter further.

A copy of this letter goes to Julia Giese and Bradley Speigner at the Bank of England, to Vanessa MacDougall and Daniel Gallagher at the Treasury and to Jonathan Athrow and Darren Morgan here at ONS.

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<sup>3</sup> For more information on these changes please see Mike Prestwood's previous letter of 7<sup>th</sup> November 2016: <https://www.ons.gov.uk/economy/inflationandpriceindices/methodologies/notificationofproposedchangestorpiin2017> and the impact article <https://www.ons.gov.uk/economy/inflationandpriceindices/methodologies/assessingtheimpactofmethodologicalimprovementsontheconsumerpricesindex>

Yours sincerely

Mike Hardie