Office for National Statistics

Consultation

National Statistician's consultation on options for improving the Retail Prices Index

Feedback form

October 2012

In responding to the consultation it would be helpful if you could use this feedback form to answer the following questions

The National Statistician's consultation on options for improving the Retail Prices Index can be found in the following link: http://www.ons.gov.uk/ons/about-ons/user-engagement/consultations-and-surveys/national-statistician-s-consultation-on-options-for-improving-the-retail-prices-index/index.html

a) Options for improving the Retail Price Index

Which option proposed would you prefer? Please enter ✓ in the box to indicate your response	
Option 1) No change. The reasons for the formula effect have been identified, explained and understood.	✓
Option 2) Stop using the Carli to estimate price change for clothing, with options of the method to be used in its place. This would reduce but not remove the formula effect as some differences between the RPI and CPI formulation would remain.	☐ If you support this option which formula do you prefer? ☐ Dutot ☐ Jevons
Option 3) Stop using the Carli for all items in the RPI. Replacing the Carli with either the Dutot or the Jevons would reduce the formula effect to a minimum, although some difference between the RPI and CPI formulation would remain.	☐ If you support this option which formula do you prefer? ☐ Dutot ☐ Jevons
Option 4) Change the RPI so that its formulae align fully with those used in the CPI. This would remove the formula effect between the RPI and CPI, though there would remain differences in estimates because of the different coverage, weights and scope used in each.	☐

What are the methodological considerations behind your preference?

This reply is from the Association of British Airways Pensioners, a lobby group for BA Pensioners.

There were, as of 2011, 98,590 BA pensioners (including dependents and deferred pensions), whose BA pensions have The Annual Review Orders (currently the CPI rise) applied as their annual inflation increase. Our needs are to have an increase that best reflects the rise in our cost of living. The gap between CPI and RPI is too big but work should be done on both indices to reduce this gap.

The overriding view of ABAP members is that the generally higher RPI rises better reflect ABAP members' cost of living than the lower CPI rises. We are therefore not convinced any of the proposed new RPIs, which would have annual rises closer to the CPI rise, would better reflect our cost of living increases. We therefore currently want the current RPI to continue and we aspire for our pension increases to be again based on RPI, not CPI.

In summary:

- The ONS should be looking at accuracy of CPI as well, not just RPI.

- It is wrong to assume CPI is right, RPI is wrong and therefore only change RPI.

- If we do change RPI, it is hard to defend the "Carli" method.

- However, we are not convinced the Jevons (geometric mean) should be used in CPI or RPI

- We need to get an index that is the best measure of how our costs are rising; the discussion paper does not address this. Ideally work should be done on both RPI and CPI to make them as close as they are in most other countries (a gap in the annual rises of around 0.2 , not the current 1.0, percentage points?)

It is seen by many of our members as cynical to have 2 indices and generally, as happens now, for HMG to use the better one, depending on whether HMG is paying out or is being paid. It is also generally seen as cynical for HMG to go for a redefined, lower-rise RPI, closer to CPI, because that is overall better for HMG's balance sheet. We agree that ONS is independent of HMG interference, but this paper does appear to be promoting a view that HMG would favour.

There is an implicit assumption in the paper that the CPI calculations are right and some of the RPI calculations are wrong, hence the need to change just some RPI calculations but leave CPI alone. As CPI is now the "headline" index, the one used for a probable majority

and growing number of inflation decisions, CPI should also be an index we get more correct.

Our pensions used to change with RPI. They now change with CPI. We want the index used to be the best fit on how UK consumer expenditure rises.

The discussion paper does not comment on the accuracy of CPI, RPI or any of the proposed modified RPIs as measures of the rise in Consumer Expenditure, or Retail Prices in the UK over the years. It only looks at the gap between the various proposed RPIs and CPI. Should we not calibrate CPI v RPI over say the last, say, 15 years and compare them with the actual spend that would have been required on a sensible, representative basket of goods? This would give a guide as to which of CPI and RPI is the better measure in inflation decisions such as pensions, and hence point to possible improvements in both the CPI and RPI measurements.

The discussion paper argues, with strong evidence, that Carli is not fit for any index: it has an upward bias and fails the reversibility test. However the practical effect of this flaw is not estimated, only academic examples are used, so the flaw might turn out to have an insignificant effect.

The formula effect gap had traditionally been 0.5% but this is now around 1.0% (Figure 2), the rise being mainly due to more accurate and detailed clothes costs from 2010. Moving from Carli, when used, to Dutot or Jevons has the same effect, by eye. From these graphs, the gap between RPI and CPI would fall by about 0.35% (Figures 3, 4) if we move from Carli on just clothing, and the gap would fall by about 0.7% (Figures 5, 6) if we move from Carli on all items, not just clothing. Therefore, we assume the current gap between RPI and CPI annual rises would move from the current 1.0% to 0.65% (if Carli were dropped for clothing only) or to 0.3% (if Carli were dropped for all items where it is used).

We agree Carli should probably be replaced by Dutot or Jevons (we later argue against Jevons however) on all the items where it is used. This begs the question as to whether RPI rises have generally been too high in the past, in fact since RPI started in 1947, or have RPI rises been too large only recently?

The worked examples on apple prices (Table D3) show the Carli upwards bias and the closeness of Dutot and Jevons to each other. However, in these examples, prices are all in the range 0.78 to 1.20. Clothing currently accounts for about half of the formula effect gap, this had became bigger when clothing data was improved in 2010; the data improvement had increased the upper quartile prices (Annex F). The range of prices for a clothing category (eg Women's dresses) will be far wider than the range in the apples prices example. Does the use of not only Carli, but also its suggested replacement, Dutot or Jevons, become far less valid due to the wide clothing price ranges? We do not know the clothing stratification strategy used, but should there not be, for example, a "full price" woman's dress and a "sale price" women's dress category, each with its own Dutot/Jevons calculated price rise and then a weighted formula, based on historical consumption, used

to get an average women's dress price rise? The same argument goes for all other clothing items, indeed any other items, with large price ranges.

We are not convinced on the suitability of Jevons anywhere. One Jevons feature pointed out is that if one of the prices is zero, the geometric mean of the prices is zero, whatever the value of the other prices. Would not a very low price (eg of clothes in a sale), effectively approaching zero in comparison to the magnitude of the other prices, then produce a geometric mean that is too close to zero, or at least not very dependent on the other non-zero prices?

A criticism of the Dutot is that it "becomes increasingly arbitrary as the set of products becomes more diverse". However, Dutot gives similar results in the graphs to those when Jevons is used, so does the Jevons have the same fault, or does this arbitrary factor have little practical effect?

Although the examples and graphs based on actual data show the effects of moving from Carli to Dutot or to Jevons are roughly the same, no mention is made of the downward bias of Jevons itself. It is mathematically impossible for a Jevons rise to be greater than a Dutot rise; the argument is that the Jevons rise being slightly smaller is due to a trading down in demand to lower priced goods (eg cheaper apples) when prices rise. How consistent is this with any implied price elasticities? Playing around with a few very simple examples, we cannot see any one price elasticity assumption that is consistent with the Jevons geometric mean calculation.

We think CPI should also be made more accurate, as well as RPI. Given ONS is currently looking at RPI though, there is a strong case for moving from Carli (when it is used) to Dutot (not to Jevons). Wide price-range items such as clothing should be stratified into different subgroups, with weightings applied to the subgroup price rises to calculate the overall price rise; we should not use a (formerly Carli but now Dutot) average price calculation over all the group, but only within each subgroup. Work needs to be done to see which of the current CPI and proposed RPIs is the better fit over the last, say, 15 years to actual expenditure on a basket of goods.

We therefore prefer:

"Option 1) No change. The reasons for the formula effect have been identified, explained and understood".

This is because we wish to improve CPI at the same time as improving RPI. However we do not yet think the reasons for the formula effect have been "identified, explained and understood". More work needs to be done here. We are as yet unconvinced that the gap between CPI and RPI rises is due to RPI being wrong and, implicitly, CPI being right.

Do the options for improving the RPI have any impacts you would like to make the National Statistician aware of?

The proposals imply RPI will be changed; we will not keep an "RPI-old", but would that not be needed, for example, for Index Linked Gilts? Correcting any error introduced after the Index Linked Gilts were sold is one thing (for example, the clothing effect) but going beyond that seems wrong.

There are probably groups with a vested interest in RPI who have not been told of the proposed changes and anyway would not generally understand this necessarily very technical paper, for example some people with National Savings. There needs to be a non-technical explanation to them with an estimate on how their investment income would reduce in the future.

b) Private housing rentals

Do you support the proposal to change the source for the data for private housing rental prices?	
YES ✓	NO ☐
Please provide any comments you would like to make in respect of this proposed change:	

c) Any additional comments

Please use this space provided for any additional comments.	
Name	**Ian Heath**
Organisation (if applicable)	**Association of British Airways Pensioners (ABAP)**

Telephone number	**01784 437679**
Email address	**i.heath@ntlworld.com**
Postal address	**1, The Elms, Falconwood, Egham, TW20 0LS**

Are you content for your response to be made public?
Please enter ✓ in the box to indicate your response:

- [x] Yes I am content for my response to be made public
- [ ] No I want my response to remain confidential

Would you like an individual response?
Please enter ✓ in the box to indicate your response:

- [ ] Yes I would like an individual response
- [x] No I am happy to receive a summary of responses

Is this a personal response or on behalf of an organisation?
Please enter ✓ in the box to indicate your response:

- [ ] Personal response
- [x] On behalf of an organisation (please state which organisation above)

If on behalf of an organisation, please state how the views of the members were assembled:

We posted a link to the ONS documents on the ABAP website and asked for feedback from ABAP members. This feedback and the ABAP committee's view lead to a draft reply we posted on the website on 24Nov2012, asking for further comments. Our final reply was hence agreed and will be published on our website by 30Nov2012

Please respond by email or post to:

Responses to the consultation can be submitted by email to: RPIConsultation@ons.gsi.gov.uk

Alternatively, responses can be sent to:

National Statistician (RPI consultation)
Government Buildings
Cardiff Road
Newport
South Wales
NP10 8XG

Please submit your response by **30 November 2012**.

Thank you for taking the time to take part in the consultation. Individual responses will not be acknowledged unless specifically requested.

Confidentiality and data protection

Information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 and the Environmental Information Regulations 2004).

If you would like the information, including personal data, that you submit to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, among other things, with obligations of confidence. In view of this it would be helpful if you could explain to ONS why you regard the information as confidential. If ONS receives a request for disclosure of the information ONS will take full account of your explanation, but cannot give an assurance that confidentiality can be maintained in all circumstances. Before disclosing any information that is personal to you, ONS will inform you of this in advance of any disclosure. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on ONS.

If you would prefer for your response and your name to be kept confidential, please make this clear in your response. Confidential responses will be included in any summary of comments received and views expressed.

Consultation timetable

This consultation will run from 8 October to 30 November 2012.

After the consultation

A response to the consultation, with a summary of the responses provided, will be published within 12 weeks of the consultation closing.

How to comment on the consultation process

If you would like to make any comments about the consultation process ONS has followed, please contact:

Lyn Hawkins, Consultations Co-ordinator
Office for National Statistics
Room 1.101
Government Buildings
Cardiff Road
Newport
NP10 8XG