



HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

4 September 2019

The Rt Hon the Lord Forsyth of Drumlean
Chairman of the Economic Affairs Committee
House of Lords
London SW1A 0PW

Dear Michael,

I am writing to respond to the Committee's inquiry into the Retail Prices Index (RPI). I am grateful to the Committee for its report and the detailed work that has been undertaken to consider RPI and its uses.

The issues your report raises are complex and wide-ranging, tackling one of the most important factors underpinning government policy-making – credible, reliable and accurate statistics. The breadth, complexity, and importance of the issues has meant that your report has required careful consideration jointly with the UK Statistics Authority (UKSA), and as a result the Government has not been in a position to respond sooner.

RPI

Your report was critical of the authorities for allowing the flaws in RPI to remain unaddressed. It concluded that UKSA, who under the Statistics and Registration Service Act 2007 are the sole body who can recommend changes to RPI, should propose a 'fix' to RPI. My consent is required for certain changes to RPI, and your report notes that my consent is only required up to 2030.

Since your report was published, the UKSA Board has made a proposal to fix RPI. UKSA have chosen to publish their proposal today. Specifically, they have proposed that RPI's methodology should be aligned with the Consumer Prices Index including owner occupiers' housing costs (CPIH). UKSA has signalled that, while it cannot commit its successors, it is unlikely that the UKSA in 2030 would take a different view from its proposal to align RPI with CPIH.

As set out in my letter today to the Chair of the UKSA, I can see the statistical arguments for UKSA's proposal to fix RPI. In coming to a decision, I consider the effect of doing so on the integrity of the statistical system, and the effects on the public finances and on the holders of specific index-linked gilts.



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There would be significant effects of UKSA's approach for users of RPI and the authorities do not know the full extent of the effects. Given this, it must be appropriate that the private and public sectors, household, firms and financial markets will need substantial time to prepare.

Therefore, I am unable to consent to the introduction of the change UKSA have proposed any earlier than February 2025, based on the information I have available. To ensure better information about the potential effects, the Government will consult publicly on whether this change should be made at a date other than 2030, and if so, when between 2025 and 2030. As part of this consultation, UKSA will consult on technical matters concerning how to implement the proposed alignment of RPI with CPIH.

The next few months are a critical period for the UK as we ready ourselves to leave the EU on 31 October, and I want to ensure that the Treasury, alongside the rest of government, has the time and space to focus on delivering Brexit. Therefore, the Government and UKSA will begin our consultation in January 2020, and we will publish a response to the consultation before the Spring Statement and the end of the financial year.

A single general measure of inflation and index shopping

Your report recommends that the Government address the imbalance in its use of consumer price indices and that in the future, one general measure of inflation is used for all purposes. The Committee's report was also critical of the Government's use of different inflation measures for different policy areas.

As the report acknowledged, the Government has made some changes in its use of inflation indices over the past decade in areas of public policy. Over this period, CPIH has also been developed, and regained its status as a National Statistic in 2017. The proposal from UKSA to change RPI is a further development in the inflation statistics landscape.

As set out at Budget 2018, the Government views CPIH as conceptually the best measure of inflation and the Government's objective is that CPIH will become its headline measure over time. The Government will continue to consider its use of RPI further at future fiscal events, drawing on the evidence gleaned in the consultation, and considering the issues in the round.

Gilts

The Committee recommended that the Government begin to issue gilts linked to CPI and to stop issuing RPI-linked gilts. The Debt Management Office (DMO) consulted on issuing CPI-linked gilts in 2011, but decided against doing so at that time. Respondents highlighted



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concerns over the demand for CPI-linked gilts, which could limit their cost-effectiveness. These factors pointed to the continuing issuance of RPI-linked gilts as the most cost-effective way of selling inflation-indexed debt at the time.

Following today's announcement of UKSA's proposal to align RPI with CPIH, and the intention to consult on the timing, I can confirm that the Government has no current plans to stop issuing gilts linked to RPI.

Long-term future of RPI

Your report recommends that once a single general measure is established, the Government should decide whether UKSA should continue publishing RPI in its existing form for RPI-linked contracts or whether a programme of adjustments should be made to RPI so that it converges to the single general measure. Given the UKSA have today proposed aligning RPI with CPIH and the widespread use of RPI across the economy, I have rejected their proposal to promote legislation to remove the requirement on the UKSA to publish RPI.

I would like to thank you again for your Committee's examination of the UK's inflation statistics landscape.

A handwritten signature in blue ink, appearing to read 'S. Javid'.

SAJID JAVID