

Press Release

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Average inflation falls, but remains high for some

Older and poorer households are facing much higher average inflation rates than younger and richer ones, as the former have tended to suffer most from continued high annual inflation in food and domestic energy costs, while the latter have tended to benefit most from cuts in mortgage rates and falling motor fuel bills, according to a new analysis of official data that is being launched as part of the ESRC Festival of Social Science today (9th March 2009).

Inflation figures published by the Office for National Statistics (ONS) are based on an 'average' basket of goods and services purchased by households. Different households will face different inflation rates according to their own expenditure patterns. Using more than 30 years of data on household expenditures from the Expenditure and Food Survey, along with RPI inflation data over the same period, IFS researchers have calculated household-level inflation figures and looked at how inflation varied both across and within household types.

Since peaking at 5% last September, the all-items Retail Prices Index (RPI) measure of inflation has fallen rapidly and stood at just 0.1% in January 2009, with forecasters predicting that it will soon fall below zero for the first time in around half a century. The headline inflation gives more weight to relatively high-spending households, for whom the inflation rate is currently relatively low. The average inflation rate we calculate across all households, at 2.1%, was therefore higher than the RPI rate, but down from 6.7% in September.

Despite the average inflation rate currently being so low, there is much more variation across households than last autumn. Just under one-third of households faced negative inflation rates in January 2009, but around one-quarter still faced inflation rates above 6%. This is an unusual amount of variation, arising because some very important items of spending like mortgage payments and motor fuel now have inflation rates far below zero, whilst the prices of other important items like food and domestic fuel are still much higher than a year ago.

Older and poorer households are currently facing the highest average inflation rates because they spend much more of their budget on food and fuel than other households. In January 2009, RPI food inflation was 9.9%, only a little below the 11.2% rate for food last September, while household fuel inflation was 35.1% in January, down only slightly from 39.6% in September.

By contrast, richer households, and in particular those with mortgages, now have very low inflation rates, on average below zero. Thanks to cuts in the base rate, mortgage interest inflation fell from -2.9% in September to -34.7%

Embargo

Until 13:00 Mon 9 March 2009

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in January¹. There have been other factors contributing to lower inflation for some groups: the fall in the oil price, for example, has seen the inflation rate for vehicle fuel fall from +20.7% in September to -15.4% by January. Taken together, in January 2009 the richest fifth of households had an average inflation rate of minus 1% while the poorest fifth had an average inflation rate of 5.3%.

While there are substantial differences in the average inflation rates of different groups at the moment, the differences are smaller if we look at average inflation over a longer period. Differences across groups tend to even out over time: those who have high inflation in one period are not always most badly affected (see table). Although poorer and older households currently face higher average inflation, it is not at all clear that this will persist into the future. There is only so much further base rates can fall, and announcements of imminent cuts in gas prices by some providers mean that the current high inflation rate for domestic fuel will not last much longer and may in fact turn negative. Food prices also appear to have peaked. Without another significant rise in the price of oil and other commodities, the story may therefore look very different later in the year.

Key findings

Inflation and housing tenure

- In January 2009, households with mortgages faced an average inflation rate of -2.7%, helped by the very low inflation rate for mortgage interest payments. Those with mortgages typically have quite volatile inflation rates that move with the level of interest rates – rising interest rates in 2007, for example, meant this group then faced the highest inflation rate across tenure groups.

- For other tenure groups, inflation rates are much higher: 4.7% for private renters, 4.9% for those who own outright and 6.1% for Local Authority renters. Local Authority tenants tend to be lower income households and spend more of their budget on food and fuel.

Inflation and age

- In January 2009, average annual inflation was substantially higher for older households than for younger households². All household groups aged under 50 had average inflation rates of less than 1%; those aged 30–39 had the lowest average rate, at -0.9%. By contrast, households aged 70–79 had inflation rates of 5.6% on average and those aged 80+ had an inflation rate of 7.1% on average.

- Differences across age groups tend to even out over time. Over a longer period since 1977, or since 1991, the average rates faced by different age groups have been much more similar. The age group facing the highest rates changes frequently – for example, in 2007 younger households faced higher rates than older households, but in 2008 this reversed.

Inflation and income

¹ The inflation rate for mortgage interest payments is based on a sample of Standard Variable Rates on offer from banks and building societies, which are very sensitive to interest rates. This inflation rate will not currently be appropriate for households with fixed-rate mortgages, but may reflect the eventual price cuts they will face once the fixed term ends.

² The age of the household is determined by the age of the head of house or their spouse, whichever is older.

- Average inflation for January 2009 was substantially lower for richer households than for poorer households. The richest 10% of households saw an average inflation rate of -1.3% and the second-richest an average of -0.7%, compared to 5.4% for those in the poorest tenth and 5.3% for those in the second-poorest tenth.
- Again, over longer time periods, differences across income groups are much smaller. If anything, poorer households have typically faced slightly lower average inflation rates than richer households if we look at the long-term average since 1977.
- For households in the poorest fifth of the population, those aged over 65 had an average inflation rate of 6.9%, compared to 4.5% for those under 35 in the same income group. For households in the richest fifth of the population, those over 65 had average inflation of 3.6% whilst those under 35 had average inflation of -3.6%.

Inflation and household composition

- Pensioner households³ currently have significantly higher average inflation than non-pensioner households. Pensioners living alone have the highest average rates of 5.8% for single males and 6.8% for single females, though these figures were over 9% last September. These are much higher than the rates for single male non-pensioners (2.0%) and single female non-pensioners (1.1%).

Commenting on these findings, Cormac O’Dea, Research Economist at the IFS, said “There are now very substantial gaps across different groups in terms of their average inflation rates. The circumstances needed to create these gaps – very high inflation in some important spending groups and very low inflation in others – do not arise very often but the sharp cuts in interest rates and the drop in oil prices coupled with food and household fuel prices still much higher than a year ago has created the picture we see today. This situation is unlikely to last much longer, however, and the relative position of rich and poor, and old and young could soon look very different.”

Table 1. Average annual inflation rate for different household groups, January 2009, annual averages for 2007 and 2008, and longer-term averages

Group	January 2009	2008 average	2007 average	Average 1977–2008	Average 1991–2008
All households	2.1%	5.0%	4.5%	5.9%	3.2%
Age 18–29	0.9%	4.2%	4.6%	5.9%	3.0%
Age 30–39	-0.9%	4.3%	5.4%	6.0%	3.1%
Age 40–49	0.0%	4.4%	5.1%	5.9%	3.2%
Age 50–59	1.7%	4.8%	4.3%	5.8%	3.2%
Age 60–69	3.9%	5.4%	3.8%	5.7%	3.2%
Age 70–79	5.6%	6.0%	3.8%	5.8%	3.3%
Age 80+	7.1%	6.7%	4.2%	6.0%	3.4%

Continues...

³ Those in which either the head or their spouse (or both) are of pensionable age.

Poorest 10% (income decile 1)	5.4%	5.8%	4.1%	5.7%	3.1%
Decile 2	5.3%	6.1%	4.0%	5.8%	3.2%
Decile 3	4.1%	5.6%	4.3%	5.9%	3.2%
Decile 4	3.2%	5.3%	4.4%	5.8%	3.2%
Decile 5	2.7%	5.1%	4.3%	5.8%	3.1%
Decile 6	1.6%	4.7%	4.4%	5.8%	3.2%
Decile 7	0.8%	4.6%	4.8%	5.9%	3.2%
Decile 8	0.0%	4.5%	4.8%	5.9%	3.2%
Decile 9	-0.7%	4.2%	5.1%	6.0%	3.2%
Richest 10% (decile 10)	-1.3%	3.9%	5.3%	6.1%	3.2%
Local Authority renter	6.1%	5.6%	3.6%	5.7%	3.1%
Private renter	4.7%	5.0%	3.3%	5.8%	3.2%
Owned with mortgage	-2.7%	4.1%	6.2%	6.1%	3.2%
Owned outright	4.9%	5.7%	3.5%	5.6%	3.2%
Single male (non-pensioner)	2.0%	4.9%	4.9%	6.3%	3.4%
Single female (non-pensioner)	1.1%	4.5%	5.1%	6.0%	3.2%
Lone parent	2.8%	4.8%	4.3%	5.5%	2.8%
Couple, no children	0.0%	4.4%	4.9%	5.9%	3.2%
Couple, with children	-1.1%	4.3%	5.4%	5.9%	3.1%
Single male (pensioner)	5.8%	6.2%	3.8%	6.1%	3.5%
Single female (pensioner)	6.8%	6.2%	4.0%	5.9%	3.3%
Pensioner couple	4.6%	5.8%	3.8%	5.8%	3.2%
Other type, with children	1.2%	4.6%	4.2%	5.6%	3.0%
Other type, no children	2.2%	4.8%	4.0%	5.7%	3.1%
Poorest 20%, aged under 35	4.5%	5.1%	3.7%	5.6%	2.9%
Poorest 20%, aged over 65	6.9%	6.8%	4.1%	5.8%	3.3%
Richest 20%, aged under 35	-3.6%	3.4%	6.2%	6.2%	3.1%
Richest 20%, aged over 65	3.6%	5.1%	3.7%	5.8%	3.3%

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Notes to Editors:

1. The method used to calculate these figures is described in “The inflation experience of older households” by Andrew Leicester, Cormac O’Dea and Zoë Oldfield, IFS Commentary 106 (<http://www.ifs.org.uk/comms/comm106.pdf>).
2. The all-items RPI figure for January 2009 was 0.1%, compared to an average of 2.1% for the households in our data. There is no reason to expect these numbers to be the same; in particular, the RPI figures weight the inflation rate of richer households more heavily which pulls down the RPI average compared to an average which weights all household equally.
3. These figures will be presented from 1pm to 2pm on Monday 9 March 2009, as part of the ESRC Festival of Social Science (<http://www.esrc.ac.uk/ESRCInfoCentre/FSS/>). Please let Bonnie Brimstone (020 7291 4818 / bonnie_b@ifs.org.uk) know if you wish to attend.