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OUTLOOK FOR RPI\TPI: MARCH AND APRIL 1990

March's figures

In March the RPI is expected to show a rise in the annual rate of inflation to about 8.1 per cent, from February's 7.5 per cent. This mainly reflects the latest increases in mortgage interest rates. Excluding mortgage interest payments the annual rate is likely to rise slightly to 6.3 per cent in March from February's 6.2 per cent.

2. The annual rate for the TPI is expected to increase to around 6.8 per cent, following 6.2 per cent recorded for February.

3. Between February and March the all-items RPI is expected to show an increase of some 1.0 per cent compared with 0.4 per cent over the same period a year ago. In addition to the increase in mortgage interest rates which added about 0.4 per cent to the RPI this March, there were further increases in food prices, some rises for household goods and clothing reflecting the ending of many seasonal sales discounts, and some increase in the prices of second-hand cars.

Outlook for April's RPI

4. The annual rate of inflation is likely to rise sharply in April to about 10 per cent or a little above. The index is now expected to rise by some 3.6 to 3.8 per cent between March and April, around 2 per cent more than in April 1989. There are many price rises which traditionally take place in April, but for many items the increases this year will be greater than a year ago: Community charge (compared with rates), rents and utilities and the effect of duty increases on alcohol, tobacco and petrol announced in the Budget. Some further rises are likely for milk and other food items. The annual rate excluding mortgage interest payments is likely to rise to some 8.5 to 8.7 per cent in April.

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	<u>Percentage changes</u>			
	RPI: all items		RPI excluding mortgage interest payments	TPI
	<u>over 1 month</u>	<u>over 12 months</u>	<u>over 12 months</u>	<u>over 12 months</u>
<u>1989</u>				
Sept	0.7	7.6	5.8	7.6
Oct	0.8	7.3	6.1	6.0
Nov	0.9	7.7	6.1	6.4
Dec	0.3	7.7	6.1	6.4
Jan	0.6	7.7	6.1	6.3
Feb	0.6	7.5	6.2	6.2
<u>Outlook</u>				
<u>1990</u>				
March	1.0	8.1	6.3	6.8
April (likely range)	3.5-3.7	9.9-10.1	8.4-8.6	8.2-8.4

The final figures for March will be circulated next Tuesday pm, in advance of publication on Thursday 12 April.

BRANCH E2
CSO

6 APRIL 1990



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PRIME MINISTER

RPI FOR MARCH AND PROSPECTS FOR APRIL

I have just seen the CSO's note of 6 April giving the outlook for the RPI over the next two months.

The likely outturn for March is precisely in line with our expectations. All-items RPI inflation is expected to rise to 8.1 per cent, with a small rise in the rate excluding mortgage interest payments to 6.3 per cent.

Yehorani? However, the CSO have significantly revised up their earlier forecast of the likely inflation rate in April (prepared as recently as 22 March) from a range of 9.4 - 9.6 per cent to 9.9-10.1 per cent now.

A number of factors have combined to make them more pessimistic about April's inflation outlook. Shell, Esso and Texaco have announced petrol price increases in the wake of an increase in the Rotterdam spot petrol price in the last week or so. This seems to reflect uncertainties about supply and buoyant European demand.

Another factor is that CSO have revised down their estimate of domestic rates per head last year to compared with the community charge this year. The upshot is that because the base is lower in

N.B. Then the RPI has been too high ever since last year and should be lowered retrospectively. They cannot have it both ways.



1989, the increase in community charge next month is bigger and has a larger impact on the RPI. This is a further one-off problem associated with switching from rates to community charge. We will not have the same problem next year because this year's community charge will be a fixed and unalterable base. Even so, I have asked my officials to pursue with CSO whether the downward revision to rates per head last year is justified. We shall see.

CSO have made no allowance in their April estimate for community charge capping. They are investigating their guidelines to see whether there is scope to make allowances for it by the time they actually publish the April number. As it stands the guiding principle laid down by RPIAC suggests that we have to use the current liability for community charge, and to make the actual change to the RPI when the new capped figure becomes operational. But there may still be room to take the effect into account. If there is, the April figure could be lower by up to 0.1 per cent.

But on present information inflation is still likely to be around 10 per cent in April. Such a prospect is very worrying, and there are no practical policy options to reduce this. But I am increasingly disturbed that such a key concept as the RPI is so badly defined. It includes mortgage interest payments which means that essential counter-inflationary interest rate increases perversely raise inflation. Canada apart, we are the only major country to include such effects in their measure of consumer prices.

It also includes community charge, which arguably it should not. And the RPIAC, whose recommendations are so seemingly important to the methodology of the RPI, have a record of taking decisions which, no matter how well-meaning (or perhaps self-serving on the part of the lobbies represented), present us with great difficulties.

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These latest developments all confirm yet again the damaging consequences of being guided by such a body as the RPIAC as it is now constituted. When their current work programme is completed, I am minded to alter the composition of the Committee and I am considering other options. One approach which has attractions would be to take an initiative in the EC to investigate a measure of retail prices which might find agreement among all member countries. There must be a better way to measure them than we currently do. If you agree I could suggest this to Christopherson when next I write to him. I am sure that given the current practice in other European countries any such investigation would not endorse the inclusion of mortgage interest payments but the process of reaching agreement could be long drawn out. However, before embarking upon this course, I have asked officials to prepare an urgent note on the policy implications of a public posture that will imply we are contemplating a significant change to the RPI.

[J.M.]

6 April 1990



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