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**REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND  
THE COUNCIL**

**on the suitability of the owner-occupied housing (OOH) price index for integration into  
the harmonised index of consumer prices (HICP) coverage**

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## **1. INTRODUCTION**

Article 3(7) of Regulation (EU) No 2016/792 <sup>(1)</sup>, requires the Commission to prepare by 31 December 2018 a report assessing the suitability of the owner-occupied housing (OOH) price index for integration into the coverage of the harmonised index of consumer prices (HICP). In preparing this report, the Commission asked the European Central Bank (ECB) for its view, as the main user of the HICP, and consulted the Member States on the feasibility of providing the OOH price index in line with HICP requirements.

The HICP is a consumer price index designed to measure inflation in a harmonised manner across Member States. It was developed to be used by the Commission and the ECB to assess price stability in the Member States under Article 140 of the Treaty on the Functioning of the European Union. Before the adoption of Regulation (EU) No 2016/792, the compilation, collection and dissemination of the HICP were regulated by Regulation (EC) No 2494/95 <sup>(2)</sup> and its implementing regulations.

When the HICP was published for the first time (in 1997), there was no consensus as to whether it should cover owner-occupiers' costs. The possibility of constructing an index based on the 'net acquisition' approach was examined at the time and found to involve considerable practical difficulties for the Member States. In 2000, after consultations with the ECB, Eurostat launched a pilot project to encourage Member States to look into ways of compiling an OOH index based on that approach. The adoption of Commission Regulation (EU) No 93/2013 <sup>(3)</sup> provided a legal basis for the compilation of a standalone quarterly OOH price index based on 'net acquisition'. Subsequently, Regulation (EU) No 2016/792 introduced a requirement to compile and disseminate such an index.

This report presents the Commission's assessment, in the light of the relevant legal requirements, of the suitability of the OOH price index for integration into the HICP coverage.

## **2. HICP REQUIREMENTS**

Under Article 3(3) of Regulation (EU) No 2016/792, the HICP should cover price changes for goods and services falling within the scope of household final monetary consumption expenditure. The key point here is the focus on:

- (i) actual monetary transactions; and (ii) consumption expenditure.

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<sup>(1)</sup> Regulation (EU) No 2016/792 of the European Parliament and the Council of 11 May 2016 on harmonised indices of consumer prices and the house price index, and repealing Council Regulation (EC) No 2494/95 (OJ L 135, 24.5.2016, p. 11).

<sup>(2)</sup> Council Regulation (EC) No 2494/95 of 23 October 1995 concerning harmonised indices of consumer prices (OJ L 257, 27.10.1995, p. 1).

<sup>(3)</sup> Commission Regulation (EU) No 93/2013 of 1 February 2013 laying down detailed rules for the implementation of Council Regulation (EC) No 2494/95 concerning harmonised indices of consumer prices, as regards establishing owner-occupied housing price indices (OJ L 33, 2.2.2013, p. 14).

Article 7(1) and (3) of the Regulation require Member States to provide their full set of HICP data no later than 15 calendar days after the end of the reference month (20 calendar days for the January indices). Member States whose currency is the euro have to transmit the flash estimate of the HICP no later than the penultimate calendar day of the month to which the flash refers.

### 3. EUROSTAT'S OOH PRICE INDEX

OOH costs are the costs associated with purchasing, maintaining and living in one's own home. The main approaches to measuring the inflation faced by owner-occupiers in a consumer price index are:

- the (net) acquisition approach;
- the use approach (covering the user and rental equivalence approaches); and
- the payments approach.

All these approaches are conceptually sound, have a basis in economic theory and have strengths and weaknesses<sup>(4)</sup>. As to which method is most appropriate for measuring inflation, this depends on user needs and the purpose of the index. For the HICP, the net acquisition approach has been judged to be the most appropriate, because it is the method that most closely corresponds to the purpose of the HICP, i.e. to measure the change through time of the total expenditure associated with all actual monetary transactions made by households to acquire goods and services for consumption purposes. All other alternatives use imputations and therefore depart from actual monetary transactions. This is the main reason why Eurostat chose in 2000 to use the net acquisition approach for the OOH price index.

The net acquisition OOH price index measures changes in transaction prices in respect of dwellings that are new to the household sector, and of other goods and services that households acquire in their role as owner-occupiers. It excludes transactions between households. It comprises the following sub-indices (Article 3(1) of Regulation (EU) No 93/2013):

#### *O.1.1. Acquisition of dwellings*

##### *O.1.1.1. New dwellings*

###### *O.1.1.1.1. Purchases of new dwellings*

###### *O.1.1.1.2. Self-built dwellings and major renovations*

##### *O.1.1.2. Existing dwellings new to households*

##### *O.1.1.3. Other services related to the acquisition of dwellings*

#### *O.1.2. Ownership of dwellings*

##### *O.1.2.1. Major repairs and maintenance*

##### *O.1.2.2. Insurance connected with dwellings*

##### *O.1.2.3. Other services related to ownership of dwellings*

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<sup>(4)</sup> See chapter 1 of Eurostat's '[Technical manual on Owner-Occupied Housing and House Price Indices](#)' for an extensive discussion of the advantages and disadvantages of the various approaches.

The OOH price index excludes the value of land from the expenditure weights related to dwellings (categories O.1.1.1 and O.1.1.2), but currently takes account of the full transaction price for dwellings (i.e. the dwelling structure and the underlying land).

As required by Article 6(2) of Regulation (EU) No 2016/792, the index is compiled every quarter. It is currently released 100 days after the end of the reference quarter.

#### **4. ASSESSING THE SUITABILITY OF THE OOH PRICE INDEX FOR INCLUSION IN THE HICP**

Two kinds of criteria for assessing the suitability of the OOH price index for inclusion in the HICP emerge from the above:

- conceptual – these relate to:
  - the need to cover actual monetary transactions only; and
  - the possible extension of the scope of the HICP to include assets (dwelling structures, land); and
- practical – these refer to the feasibility of producing an index according to HICP standards of frequency and timeliness.

##### **4.1. Conceptual aspects**

The *net acquisition approach* for OOH is the only one that fulfils the requirement of being based exclusively on actual monetary transactions. As such, the net acquisition OOH price index automatically satisfies the first criterion.

However, the inclusion of the acquisition of dwellings (structures and underlying land) in the scope of the HICP is controversial. While there is general agreement that the purpose of any consumer price index is to measure changes in the prices of consumption goods and services, the concept of *consumption* is imprecise. In official statistics, views differ as to whether it should include the costs of the structure and the land that together make up the cost of acquiring dwellings:

- One view is implied in the coverage of the HICP as defined in Article 3(3) of Regulation (EU) No 2016/792: ‘household final monetary consumption expenditure’, i.e. the part of the national accounts aggregate of household consumption expenditure incurred in monetary transactions. The national accounts treat dwelling structures as produced non-financial assets and land as a non-produced non-financial asset. Hence, from the national accounts perspective, purchases of dwellings do not belong to household consumption expenditure. This means that including the net acquisition OOH would involve expanding the current coverage of the HICP;
- When the pilot project to develop an OOH price index was being prepared in 2000, Eurostat discussed with the ECB and Member States how to apply the net acquisition approach to OOH in the HICP. In those discussions, an alternative view emerged (with a perspective that differed from that of the national accounts), according to which one could regard the cost of land as investment (asset) and the cost of the structure as consumption. The rationale for this view is that, while the structure (as a sort of durable good with very long service life) will be consumed (i.e. consumption of fixed capital), the land normally remains at constant quality (except under very unusual circumstances). This view regards the net acquisition OOH as conceptually viable for integration into the HICP, but requires structure and land to be separated

for the purpose of prices and weights. It was the view taken by the ECB when consulted for the preparation of this report.

In practice, it is normally possible to separate land and structure price components only via modelling, since land and structure are usually purchased as a single package with one overall transaction price. However, deriving the separation of prices via modelling would mean that the HICP was no longer limited to actual monetary transactions. Moreover, the academic literature shows that the resulting price estimates can differ widely, depending on the underlying assumptions;

- A third view is based on an analogy with the HICP price index for actual (market) rentals, which tracks the cost of both the structure and the land belonging to dwellings that are rented out. According to this view, a case could be made for accepting the inclusion of both the structure and the land in the OOH component in the consumer price index in the same way as the price index for market rentals does. This view regards the net acquisition OOH as conceptually suitable for integration into the HICP without separating structure and land.

To conclude, integrating the net acquisition OOH would involve a departure from the HICP coverage which is derived from the national accounts. In official statistics, views differ on whether the cost of the structure and of the land (which together make up the cost of acquiring a dwelling) can be considered as consumption expenditure that can be covered in a consumer price index or should be regarded as assets and thus left out of the coverage. From a conceptual point of view, the inclusion of the cost of dwellings in the HICP therefore remains controversial.

## 4.2. Practical aspects

The OOH price index is currently compiled every quarter and released 100 days after the end of the reference quarter. To meet HICP requirements, it would have to be produced every month and released at the end of the reference month as a flash estimate and 15 days later with the full set of figures.

The information in this section is based on Member States' answers to a Eurostat review in summer 2017. The three most important OOH sub-indices (together they account for 85 % of total OOH expenditure) are discussed below in the order of their average weight in total OOH in 2010-2017 in the Member States for which data was available:

- *O.1.1.1.2. Self-built and major renovations index;*
- *O.1.1.1.1. Purchases of new dwellings index;* and
- *O.1.2.1. Major repairs and maintenance index.*

For the *Self-built and major renovations index*, the sources used by most Member States are the construction cost index, the construction output price index or a combination of the two. In most countries, these indices are produced every quarter, as provided for in Regulation (EC) No 1165/98 <sup>(5)</sup> and the Commission's proposal for a framework regulation integrating

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<sup>(5)</sup> Council Regulation (EC) No 1165/98 of 19 May 1998 concerning short-term statistics (OJ L 162, 5.6.1998, p. 1).

business statistics <sup>(6)</sup>. Only two Member States reported that they compiled a monthly construction cost or price index, but in one case the index is based partly on estimates (rather than transaction data, as required for the HICP) and in the other the timeliness is not suitable for HICP.

For the *Purchases of new dwellings index*, most Member States use administrative data sources (transaction registers). In most cases, the number of transactions over a month is seen as insufficient to produce a reliable index: the results will be much more volatile and less accurate than quarterly data. Moreover, the figures would normally be provisional up to a year after the reference month, whereas for the HICP a provisional index has to be finalised in the following month's publication (Article 9 of Regulation (EC) No 1921/2001 <sup>(7)</sup>).

The HICP timeliness requirement is even more challenging than the monthly frequency, due to the administrative schedules in registering dwelling transactions. Once notaries have concluded the final acquisition contract, it generally takes them at least two weeks (in some cases up to two months) to forward the data to the registry. This means that only a fraction of the transactions concluded in the reference month will be registered by the end of that month, reducing even further the data available to compilers.

For the *Major repairs and maintenance index*, most countries use the construction cost index, the construction output price index or a combination of the two. Therefore, the above comments in relation to the *Self-built and major renovations index* apply here too.

In conclusion:

- the *Self-built and major renovations index* and the *Major repairs and maintenance index* are based on the construction cost index and/or the construction output price index, which in the majority of Member States are produced only every quarter; and
- for the *Purchases of new dwellings index*, most Member States use administrative data sources that in some cases could allow the production of a volatile and less accurate monthly index, but this would not meet HICP timeliness requirements.

Overall, it appears unfeasible to produce an OOH index with monthly frequency and a timeliness that (even roughly) meets HICP requirements.

## 5. THE ECB'S VIEW <sup>(8)</sup>

A key requirement as regards the ECB's analyses, assessments and forecasting of inflation in the euro area is that integrating the OOH price index should deteriorate neither the frequency nor the timeliness of the HICP. The ECB notes that the OOH price index is produced only every quarter and released 100 days after the end of the reference quarter.

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<sup>(6)</sup> Commission proposal of 6 March 2017 for a Regulation of the European Parliament and of the Council on European business statistics amending Regulation (EC) No 184/2005 and repealing 10 legal acts in the field of business statistics (COM(2017) 114 final).

<sup>(7)</sup> Commission Regulation (EC) No 1921/2001 of 28 September 2001 laying down detailed rules for the implementation of Council Regulation (EC) No 2494/95 as regards minimum standards for revisions of the harmonised index of consumer prices and amending Regulation (EC) No 2602/2000 (OJ L 261, 29.9.2001, p. 49).

<sup>(8)</sup> The ECB's view was communicated to the Commission (Eurostat) by letter dated 20 September 2017 (ARES(2017) 4634173).

Furthermore, the ECB considers the inclusion of asset price developments in the HICP problematic and notes that the OOH index includes the price of land.

The ECB concludes that the integration of the OOH price index would deteriorate the current frequency and timeliness of the HICP, and would introduce an asset element. Against this background, it takes the view that the OOH price index is in practice not suitable for integration into the official HICP.

## **6. COMMISSION'S ASSESSMENT**

Given the importance of the HICP for monetary policy and in view of the ECB's needs as its main user, the Commission considers it essential that integrating the OOH price index should have no negative impact on the quality of the HICP, in particular as regards frequency and timeliness.

In a large majority of Member States, the sources used for two of the three most important OOH sub-indices are produced on a quarterly basis only. For the third, most Member States use administrative data sources that could in some cases allow the production only of a volatile, less accurate monthly index that would not meet HICP timeliness requirements.

Therefore, it appears that the OOH price index currently cannot be produced according to HICP standards of frequency and timeliness.

Moreover, including the net acquisition OOH index would involve a departure from the current definition of HICP coverage as 'household final monetary consumption expenditure that represents the part of the national accounts aggregate of household consumption expenditure incurred in monetary transactions'. In official statistics, views differ as to whether the cost of the structure and the land that together make up the cost of acquiring a dwelling can be considered as consumption expenditure that could be covered in a consumer price index or should be regarded as assets and thus left out of the coverage. From a conceptual point of view, therefore, the inclusion of the cost of dwellings in the HICP remains controversial.

Against this background, the Commission's assessment is that the OOH price index is currently not suitable for integration into the coverage of the HICP. In line with Article 3(7) of Regulation (EU) No 2016/792 and in close cooperation with the ECB, the Commission will pursue the methodological work required for the integration of the OOH price index into the HICP coverage and report to the European Parliament and to the Council on that work, as appropriate.