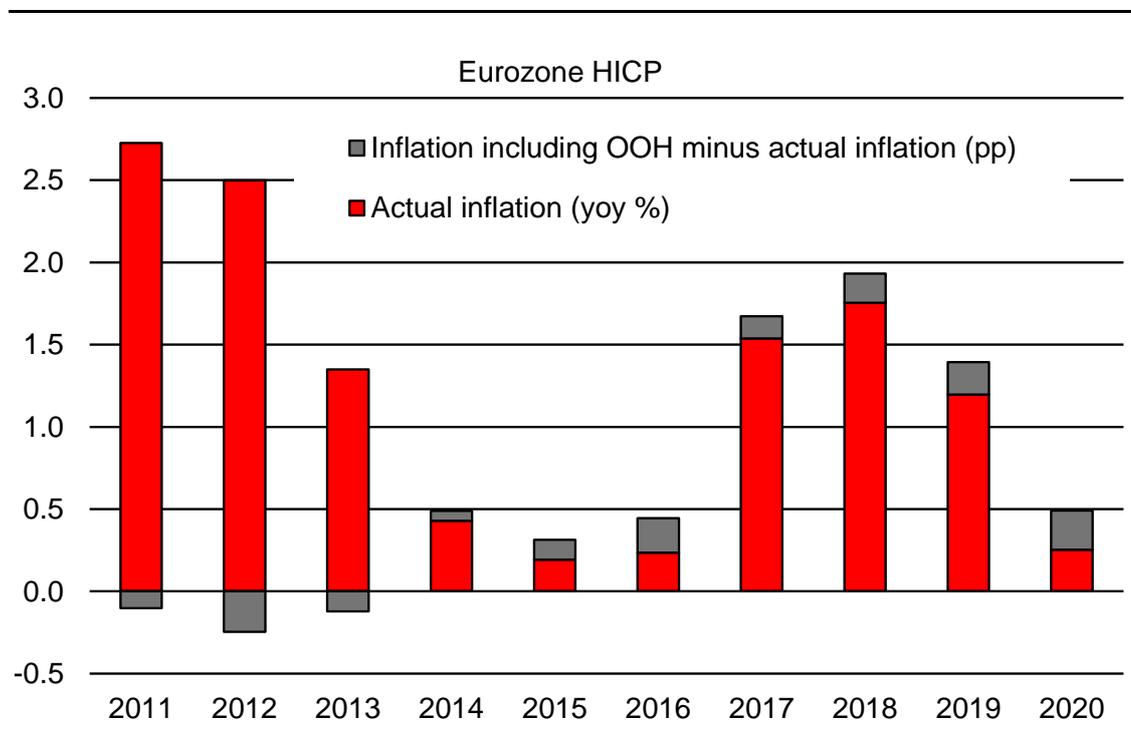


## Owner-occupied housing in eurozone HICP: Implications and challenges



Source: Eurostat, UniCredit Research

- With its strategy review, the ECB confirmed that the Harmonized Index of Consumer Prices (HICP) remains the appropriate measure for assessing the achievement of the central bank's new price-stability objective (a symmetric target of 2% inflation over the medium term). However, the Governing Council (GC) acknowledged that "the inclusion of the costs related to owner-occupied housing in the HICP would better represent the inflation rate that is relevant for households". Therefore, it recommended a roadmap to include owner-occupied housing (OOH) in the HICP.
- Our *Chart of the Week* shows an attempt to quantify the effects of including OOH in the eurozone HICP<sup>1</sup>. We make a (possibly conservative) assumption that the weight of OOH in the basket would be 10%. Over the last decade, the inclusion of OOH would have raised inflation by an average of 0.1pp per year, although the impact would have differed meaningfully over time. In 2011-13, amid weakness in the housing market, OOH subtracted from the inflation rate, while the opposite holds true in the following years, when inflation would have been 0.2pp higher, on average. This suggests two things. First, the slight increase in the target for inflation, under the new definition of price stability (to 2% from "below, but close to 2%") changes very little in practice when OOH is taken into account. Second, inflation that includes OOH might become more pro-cyclical. Using a larger weight for OOH does not materially alter the average results, but obviously increases the cyclicity of inflation.
- OOH is a tricky concept, as it reflects the costs of purchasing, maintaining and living in one's own home. Currently, housing costs in the eurozone mainly enter the HICP through actual rents, with a weight of 6.5%<sup>2</sup>, while the costs of OOH are not included. The perception by eurozone households, which we share, is that the weight of the cost of housing in the HICP basket is too low. Several advanced countries already include OOH in their inflation gauges. As a reference, in US CPI, the weight of actual rents is about 8%, while OOH accounts for most housing costs through the so-called owners' equivalent rent, with a weight of about 24%<sup>3</sup>. In the UK, the weight of costs of OOH in the CPI basket is about 16%. The main obstacle for OOH inclusion in the eurozone HICP is measurement issues, including differences in data availability and methodology in the way OOH is calculated by member states' national statistics offices. Also, OOH data are currently published with a relatively long lag – numbers for 1Q21 have only been recently published.
- The ECB's roadmap foresees four main stages for moving to an HICP including OOH costs as the main index for monetary policy purposes:
  1. The construction of an analytical index for internal purposes, which includes OOH with approximated

weights; **2** Eurostat to carry out further work on the statistical compilation of OOH weights, with the aim of publishing an experimental quarterly HICP including OOH costs in 2023; **3**. An official quarterly index to be available by 2026; **4**. OOH costs to be included in the HICP at a monthly frequency and in a timely manner (the ECB does not provide a timetable for this). During the transition period until stage 4 is accomplished, the main reference index for monetary policy will remain the current HICP, although “the quarterly OOH index will play an important supplementary role in assessing the impact of housing costs on inflation and will thus inform the GC’s monetary policy assessments”.

<sup>1</sup>Greece does not publish OOH data. For this reason, our OOH eurozone aggregate is compiled using a weighted average of all other countries’ data.

<sup>2</sup>We take 2020 weights, which better reflect pre-pandemic spending patterns.

<sup>3</sup>However, in the US PCE price index, the weight is only about half that in the CPI.

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