Article

Role of owner-occupiers' housing costs in the Household Cost Indices, UK : 2023

The impact of higher mortgage interest rates on household costs, on average and by different household subgroup

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1 . Main points

- Average UK household costs, as measured by our Household Costs Indices (HCI), increased by 5.0% in the year to December 2023, following a 12.4% increase over the same period in 2022; on a cumulative basis, household costs are up 24.7% since December 2019.

- Owner-occupiers' housing has been an important driver of this increase in household costs, which have overtaken food and energy prices as the main contribution to the annual rate of change in our Household Costs Indices (HCI).

- Households with the largest mortgages were most exposed to this increase in owner-occupiers' housing costs, which most often include working-age households with children and above-average disposable income.

- Higher savings and better financial resilience have meant mortgage holders were better able to absorb increases in housing cost compared with renters.

2 . Background

Consumer price inflation in the UK is still high, which has resulted in an increased cost of living for UK households. Our Household Cost Indices (HCIs) capture changes in the costs and prices that households are facing. The HCIs measure how much a household's disposable income would need to change, in response to changes in costs and prices, so that they could purchase the same quantity of goods and services.

There was a 5.0% increase in the HCI in the year to December 2023, for an average household. Costs are still increasing, although at a slower pace compared with a year ago. On a cumulative basis, this average HCI has increased by 24.7% since December 2019.

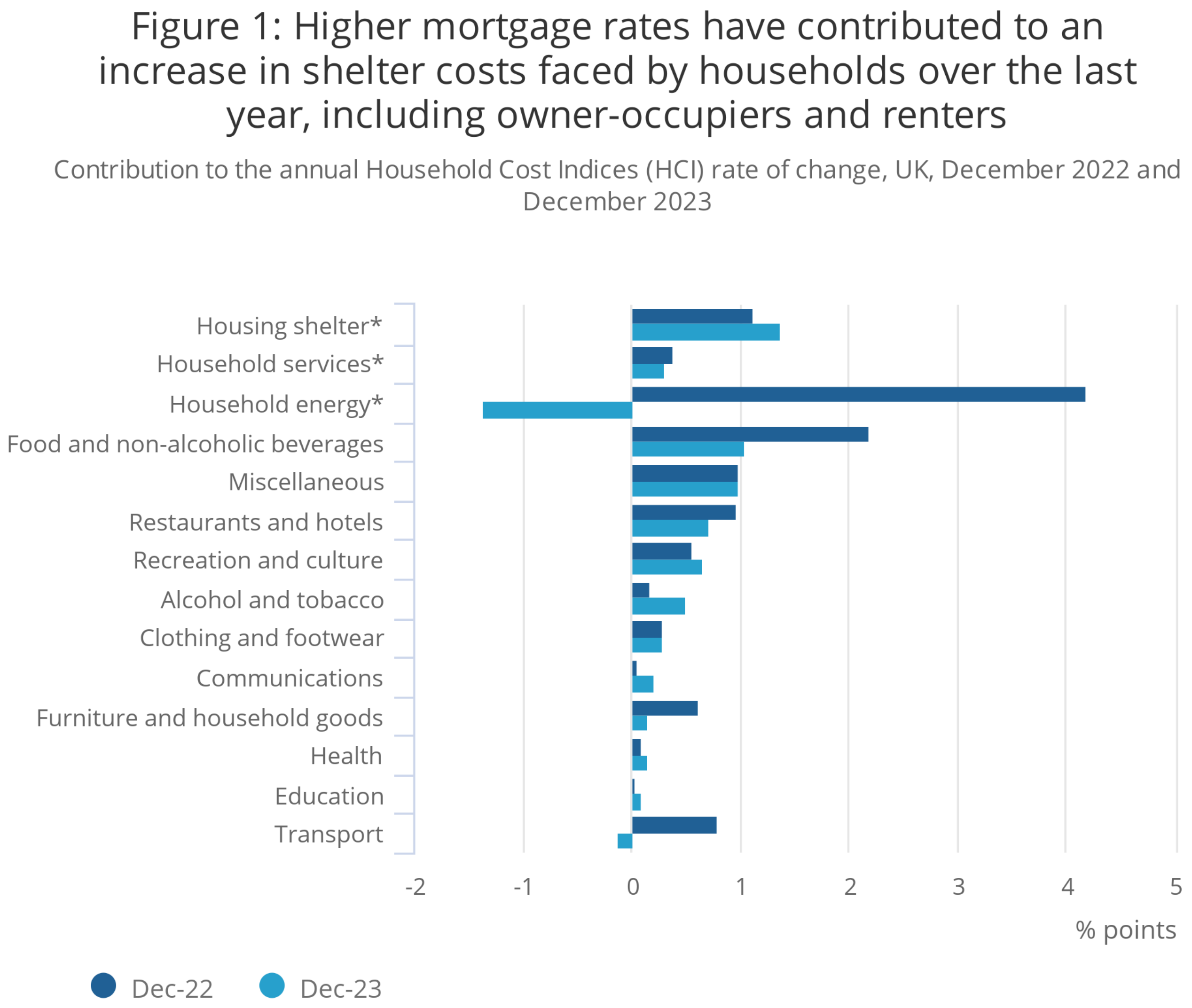
HCIs provide more insight into some of the distributional effects of these higher costs and prices, including how different types of households may change their consumption in response. This enables us to explore whether there has been an uneven impact of this period of high inflation, reflecting the varying consumption patterns of households and the ability to adjust their consumption in response to changes in prices.

Food and energy prices were initially the main driver of this increase in household costs, which comprises a higher share of consumption of low-income households. More recently, the contribution of housing costs has become increasingly substantial, overtaking food and energy as a leading driver of the annual increase in the HCIs. This was driven by the shelter component as rents and mortgage interest payments increased over the last two years (Figure 1). These payments increased as fixed-rate mortgage products that were initially locked in during the period of low interest rates then expired, so that an increasing number of households have had to remortgage at a higher interest rate. The level of house prices is still high despite this increase in interest rates, to the extent that new mortgagors (the borrower of a mortgage) still require large loans to finance their house purchases. These trends have pushed up the cost of owning a home, with some household subgroups seeing more impact than others.

The impact of higher mortgage rates will be captured by the owner-occupiers housing (OOH) component within our HCIs, where the effect on the costs and prices are likely to vary by type of household. The HCIs enable us to explore whether there are some types of households that have been more exposed to the increase in the cost of owner-occupied housing.

Figure 1: Higher mortgage rates have contributed to an increase in shelter costs faced by households over the last year, including owner-occupiers and renters

Contribution to the annual Household Cost Indices (HCI) rate of change, UK, December 2022 and December 2023



Source: Office for National Statistics

Notes:

1. Housing shelter includes private rentals, social rentals, and owner-occupiers' housing costs. Household energy includes electricity, gas, liquid, and solid fuels. Household services includes repairs of dwelling services and materials, water supply, sewage collection, council tax, and UK holiday rents. Together, housing shelter, household energy, and household services are the component parts of the Housing, Water, Electricity, Gas and Other Fuels division.

3 . The impact of higher mortgage interest payments on HCIs

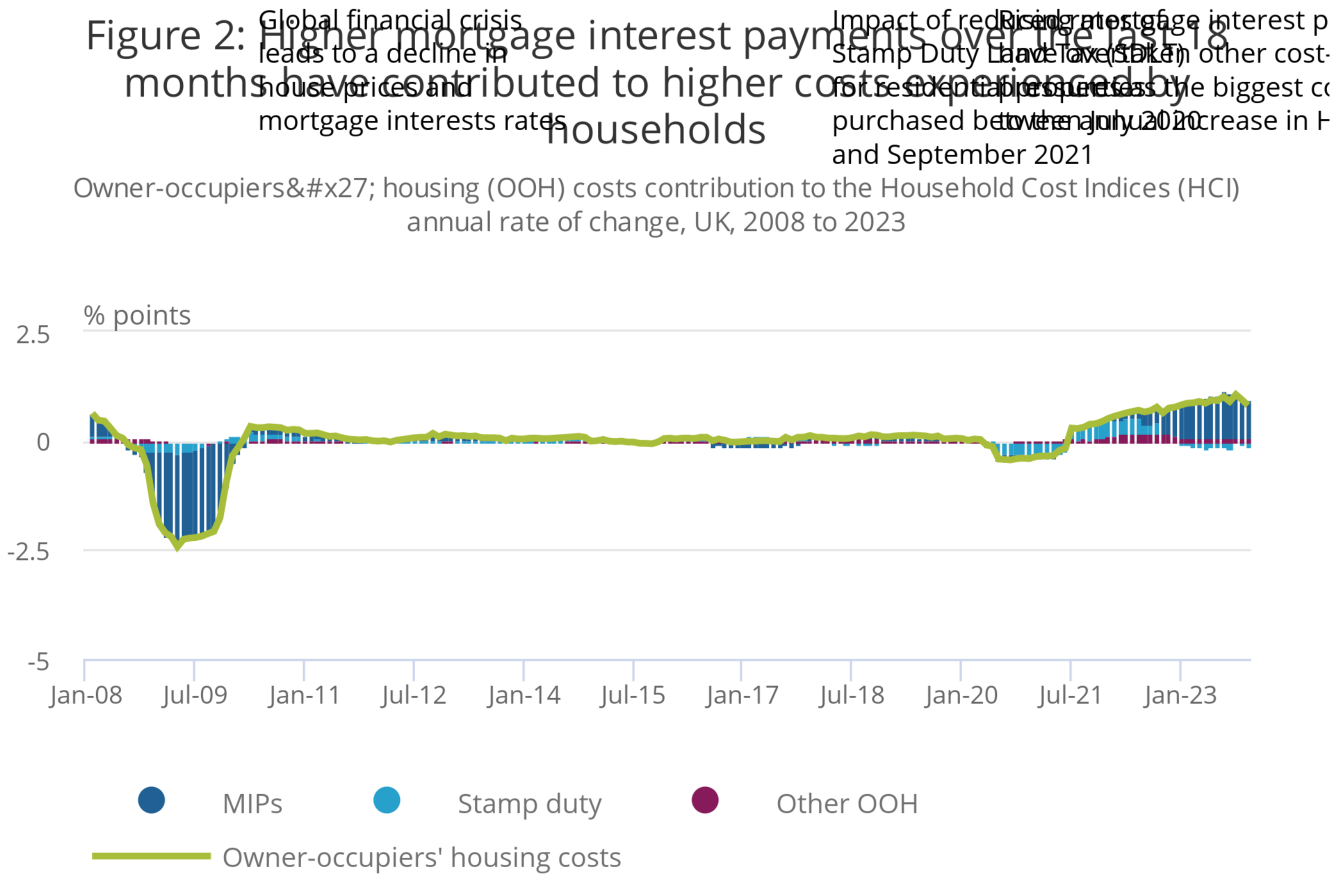
The HCIs focus on the payments made for a basket of goods, services, and other financial transactions, including how this cost and price experience varies by household. One example is owner-occupiers' household costs (OOH), which measure what it costs owner-occupiers to live in their own homes. Unlike CPIH, the HCIs are based on the payments approach, which includes changes in mortgage interest payments. These are the actual costs paid by households out of their disposable income, rather than imputed rents, which are a proxy for the cost of consuming shelter as a housing service. The payments approach also includes changes in stamp duty rates and other payments as represented by dwelling insurance, ground rent, estate agent fees, home-buyers surveys, and house conveyancing.

Figure 2 shows the role of OOH costs to the annual change in HCI for an average household over the last 15 years. There have been 2 periods where there have been relatively large changes in OOH costs. The first in 2008 and 2009, reflecting a loosening in monetary policy in response to the financial crisis, which resulted in lower mortgage interest payments. Please note that there was a methodological change during this period. Up to January 2010, the interest rate was a weighted average of the Standard Variable Rate (SVR) offered by banks and building societies. This was replaced with the Average Effective Rate (AER), which also includes other mortgage types such as fixed rate, discount, and tracker mortgages. For more information, please visit our CPI Technical Manual methodology page.

The second period has taken place over the last 18 months as there has been a tightening in monetary policy in response to higher inflation. Taken together, OOH costs increased by about 23% in the year to December 2023 according to the payments approach, contributing 0.8 percentage points to cost inflation over the same period for an average household.

Figure 2: Higher mortgage interest payments over the last 18 months have contributed to higher costs experienced by households

Owner-occupiers' housing (OOH) costs contribution to the Household Cost Indices (HCI) annual rate of change, UK, 2008 to 2023



Source: Office for National Statistics

Notes:

1. MIPs denotes mortgage interest payments.

Higher mortgage interest payments (MIPs) were the main driver of this increase in OOH costs, mainly driven by higher interest rates and partly by the increase in house prices following the coronavirus (COVID-19) pandemic, which meant that owner-occupiers needed to take up larger mortgages and provide larger deposits to achieve the same loan-to-value ratios.

Stamp duty rates were another driver of owner-occupiers housing costs in recent years. The stamp duty holiday during the pandemic subtracted on average about 0.3 percentage points from annual cost inflation between July 2020 and June 2021. The stamp duty holiday was introduced in July 2020 to stimulate the housing market during the pandemic. The tax break meant buyers were exempt from stamp duty for properties below £500,000, resulting in potential savings of up to £15,000. Initially it was set to end in March 2021, but was extended to July 2021, before being phased out and withdrawn totally in September 2021.

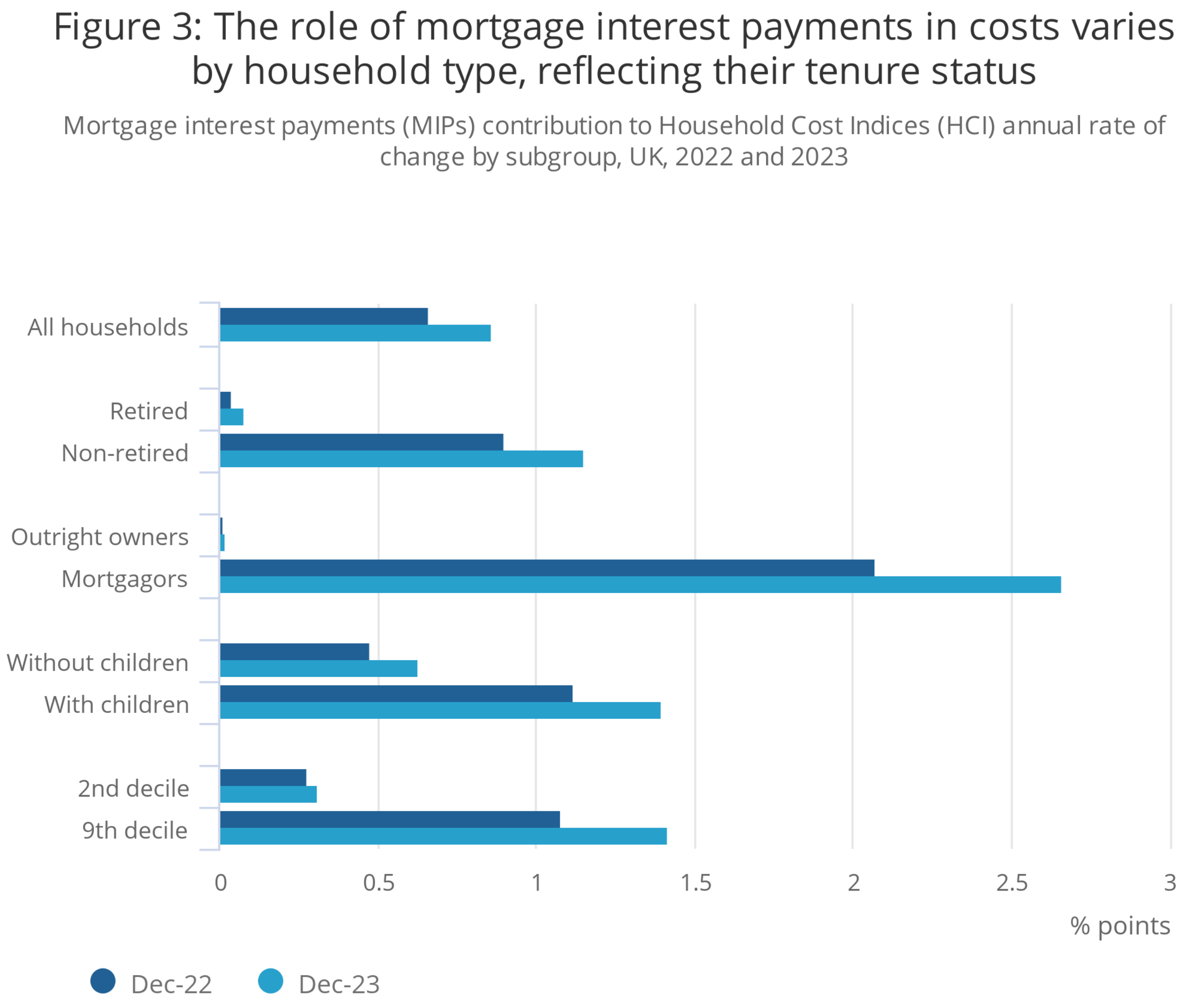
The subsequent phasing out of the stamp duty holiday - together with base effects from the previous reduction in stamp duty rates - pushed up annual HCI inflation between July 2021 and September 2022 by a similar amount. More recently, the contribution of stamp duty rates has turned negative owing to our house price index edging lower in 2023 - for more information, please see our [UK House Price Index: December 2023 bulletin](#).

The contribution of Other OOH - dwelling insurance, ground rent, estate agent fees, home-buyers surveys, and house conveyancing - was generally small owing to its low weighting within our HCIs. It has seen some increase in recent years as rising costs of labour and materials pushed up insurance premiums while changes in market regulation reduced the discounts insurers could give to new customers compared with their existing business. Similarly, the strength of the housing market during the pandemic pushed up estate agent, surveyor, and conveyancing fees. Ground rent has also increased, which might reflect higher land and property prices.

The contribution of MIPs is about zero for outright owners, as they do not pay mortgage interest, although a few might have loans on second homes. In comparison, the contribution of MIPs for mortgagors was 2.7 percentage points in the year to December 2023 (Figure 3), up from 2.1 percentage points in the year to December 2022. Such differences in housing tenure status also explain much of the difference in the MIPs' contribution to the annual increase in costs for retired and non-retired households, for households with and without children, and for households by different income deciles (Figure 3).

Figure 3: The role of mortgage interest payments in costs varies by household type, reflecting their tenure status

Mortgage interest payments (MIPs) contribution to Household Cost Indices (HCI) annual rate of change by subgroup, UK, 2022 and 2023



Source: Office for National Statistics

Table 1 shows that the share of mortgagors is larger among higher-income households (9th income decile at 46%) than among lower-income households (2nd income decile at 15%). This is to be expected as high-income households typically have better access to mortgage finance and can more easily save for a house deposit. Mortgagors are also usually of working age as retirees have in most cases paid back their mortgages. Also, mortgagors at lower and middle incomes are typically more likely to live with children while high-income mortgagors are more likely to live without children. Lower-income households more often tend to be renters (41%) than mortgagors (15%). They are also often owner-occupiers in the case of retirees on pensions that rank them at the lower end of the overall income distribution.

Table 1: The share of mortgagors is larger among higher-income households than among lower-income households
Tenure status of different household groups

% of total	Mortgagor	Outright owner	Private renter	Social renter
Retired	3%	79%	5%	13%
Non-retired	42%	20%	22%	37%
With children	51%	10%	20%	18%
Without children	23%	46%	17%	14%
2nd decile	15%	44%	19%	22%
5th decile	31%	34%	16%	18%
9th decile	46%	33%	17%	4%

Source: Office for National Statistics

Notes

1. Deciles refer to household equivalised disposable income.

One factor that could help higher-income households absorb the increase in mortgage interest payments is that they typically have a higher savings than lower-income households. Our Opinion and Lifestyle Survey shows a higher share of renters (46%) than mortgage holders (36%) reported finding it difficult to afford their rent or mortgage, despite mortgage interest payments having increased by more than rents in our HCIs. One potential explanation is that mortgagors, on average have more disposable income than renters, to manage increases in costs. Similarly, mortgagors spend a lower share of their disposable income on mortgage interest payments compared with the share of income that renters spend on paying rent.

Our Wealth and Asset Survey also suggests that a lower share of household who rent (52%) were financially resilient compared with mortgagors (78%) and outright owners (93%), where financial resilience was measured as having sufficient savings to cover a quarter fall in employment income over a three-month period. For more information on distribution of cost-of-living pressures across different populations, see our Impact of increased cost of living on adults across Great Britain article.

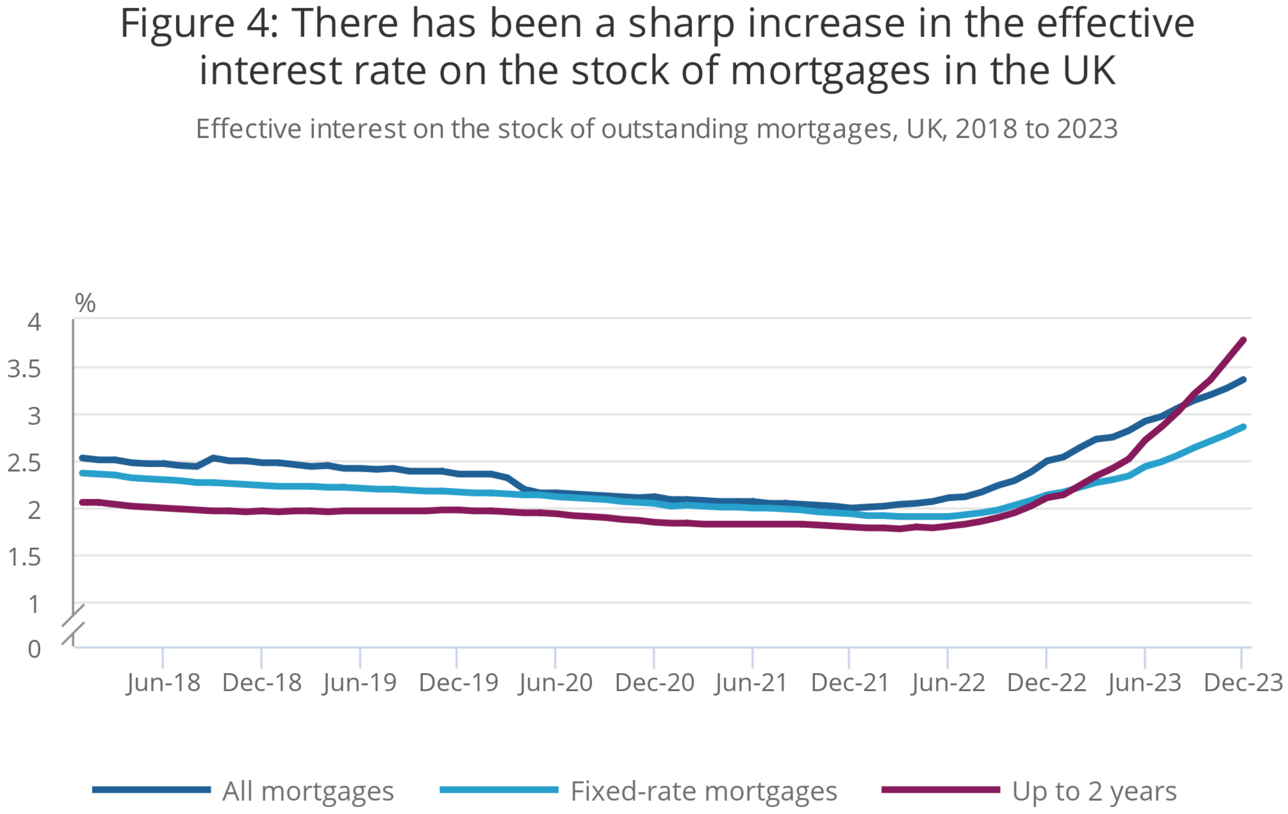
4 . The pass-through of higher interest rates into mortgages and time deposits

The increase in the contribution of MIPs to annual HCI inflation in recent years has mainly been driven by higher mortgage rates. The extent to which higher interest rates will feed into mortgage rates will reflect the composition of fixed- and variable-rate mortgages in the UK economy, which has changed over time. For instance, fixed-rate mortgages accounted for 88% of total mortgages outstanding in Quarter 4 2023, of these 26% are fixed for up to 2 years and 68% are fixed for up to five years.

The effective rate on the stock of mortgages outstanding has increased to about 3.4% in December 2023 from around 2.1% during the coronavirus (COVID-19) pandemic (Figure 4). A part of the increase in mortgage interest payments was also driven by higher house prices as the average UK house price, as reported in our [UK House Price Index: December 2023 bulletin](), increased by about 23% over the four years to December 2023. This means that mortgagors are now borrowing larger amounts to finance their house purchases, compared with pre-pandemic levels.

Figure 4: There has been a sharp increase in the effective interest rate on the stock of mortgages in the UK

Effective interest on the stock of outstanding mortgages, UK, 2018 to 2023



Source: Bank of England, Office for National Statistics

Mortgage interest payments will continue to increase as long as interest rates on new mortgages remain above the effective interest rate on the outstanding mortgage stock. For example, about 25% of mortgagors, currently paying fixed-rate mortgages, will reach the end of fixed-rate periods (also known as "fixes") within the next two years. Their average interest rate was around 3.8% in December. If these households were to remortgage at quoted market rates as of January 2024, their quoted interest rates would usually be between 4% and 7%, depending on their loan-to-value (LTV) ratio and whether they opt for a two-year or five-year fixed rate (see Table 3). This would push up the effective interest rates on outstanding mortgages, leading to higher average household mortgage interest payments, and therefore further increasing the household cost indices (HCI).

Table 2: Quoted household interest rates on fixed mortgages
By loan-to-value ratio and period of interest rate fixation

%, January 2024	60% LTV	75% LTV	90% LTV	95% LTV
2-year fixed rate	4.6	4.7	5.4	5.9
5-year fixed rate	4.3	4.4	4.8	5.2

Source: Bank of England, Office for National Statistics

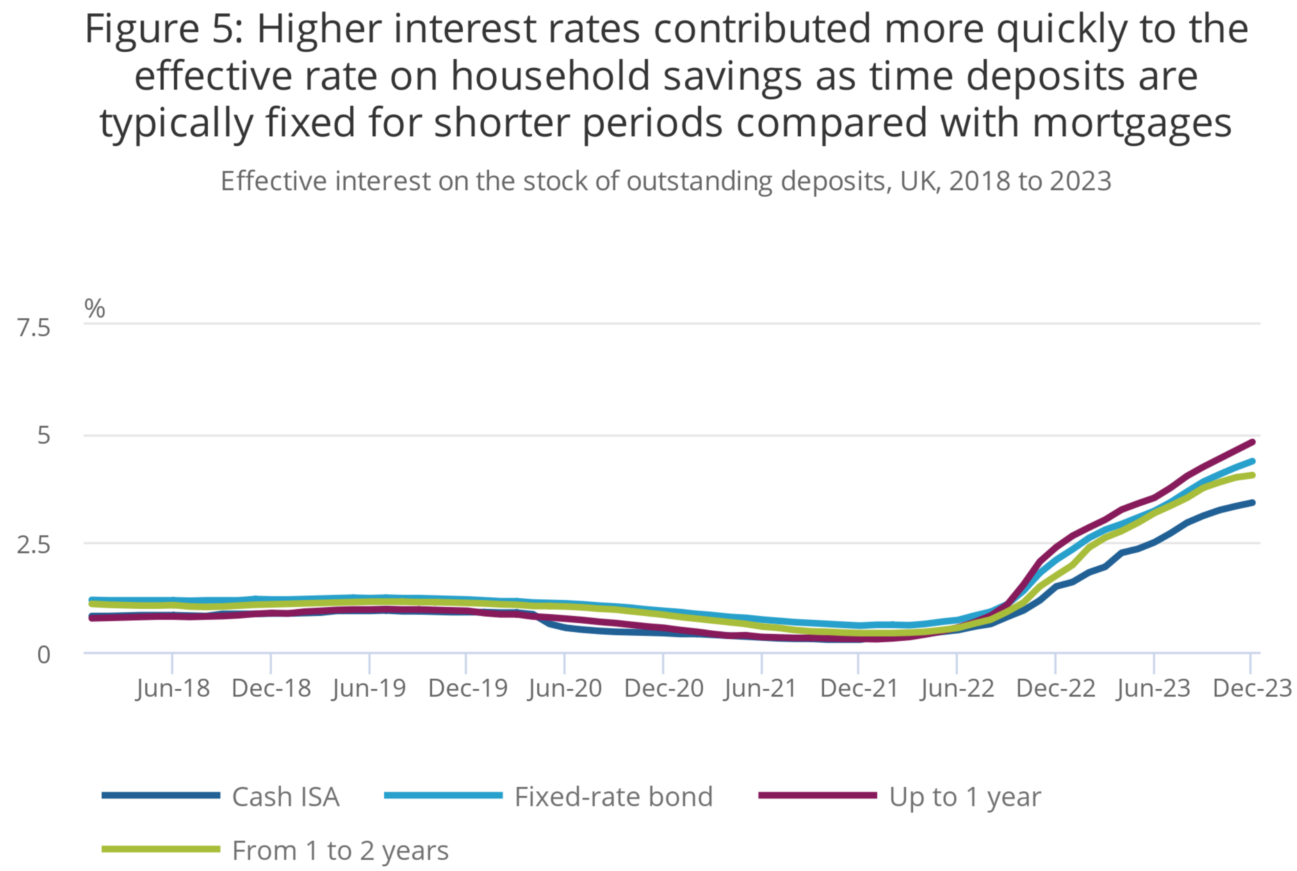
Notes

1. Quoted interest rate series are calculated monthly by the Bank of England, as weighted averages for a range of lending products offered to households.

The impact of higher mortgage interest payments on household consumption might be partly offset by higher income on households' savings as interest rates paid on time deposits also increased (Figure 5). The pass-through of higher interest rates into the stock of outstanding time deposits accelerated last year compared with mortgages, as rates on time deposits are typically fixed for a shorter period.

Figure 5: Higher interest rates contributed more quickly to the effective rate on household savings as time deposits are typically fixed for shorter periods compared with mortgages

Effective interest on the stock of outstanding deposits, UK, 2018 to 2023

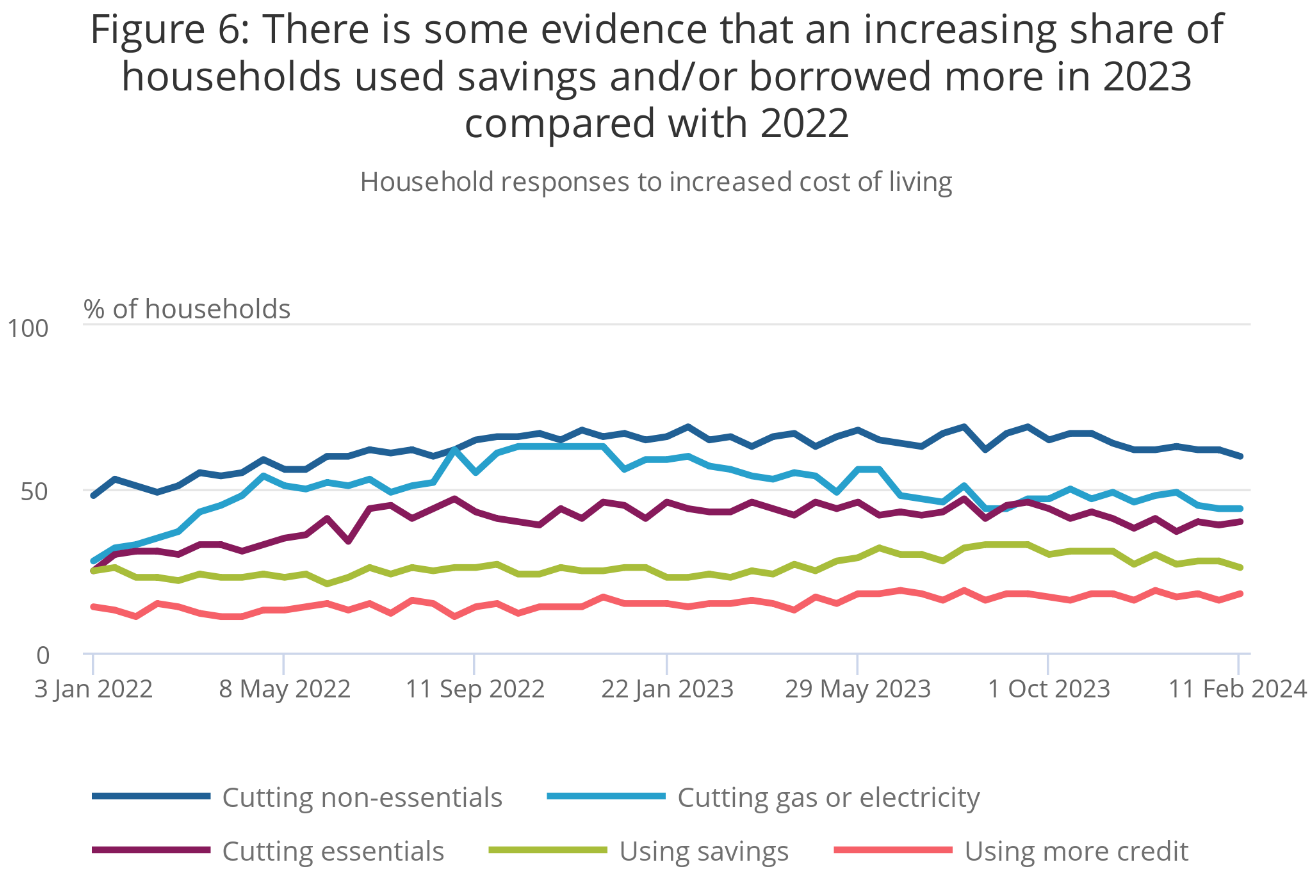


Source: Bank of England, Office for National Statistics

The benefits of the increase in savings rates and the costs of higher mortgage payments will accrue to different household groups, depending on their individual financial situation and whether a household is a net lender or a net borrower. Our Opinions and Lifestyle Survey suggests that a higher share of households may have used their savings and/or borrowed more in 2023 compared with 2022, as a response to higher cost of living. However, the dissaving rate, that is the rate at which households used or withdrew their savings, slowed slightly in recent months (Figure 6). Low-income households more frequently reported using credit and less frequently reported using savings relative to high-income households.

Figure 6: There is some evidence that an increasing share of households used savings and/or borrowed more in 2023 compared with 2022

Household responses to increased cost of living



Source: Office for National Statistics

Notes:

1. Dates denote last day of reference period.

2. Data may have some breaks as the questionnaire evolved over time.

5 . Glossary

Disposable income deciles

Households are grouped into deciles (or tenths) based on their equivalised disposable income. The richest decile (decile 10) is the 10% of households with the highest equivalised disposable income. Similarly, the poorest decile (decile 1) is the 10% of households with the lowest equivalised disposable income. It should be noted that the second and ninth deciles are more stable, so users may wish to consider these in their analysis.

Households with children

A child is defined as any person aged under 16 years. For the purposes of the Family Spending report, people who are aged under 18 years and unmarried are also classed as children. A household is classified as a household with children if at least one member of the household is a child.

Outright owner-occupier households

Owner-occupier households are defined as any household in which the residents own the property outright and use it as their primary or non-primary residence.

Mortgagor and other owner-occupier households

Owner-occupier households are defined as any household that is buying their primary or non-primary residence property with a mortgage, or own part of the property (for example, paying both rent and mortgage).

Renter households

A renter household is defined as any household that rents their property from a private sector landlord. It excludes households who live in their property rent free.

Social and other renter households

Non-private renter households are defined as any household that rents their property from a council or a registered social landlord or lives in their property rent free.

Retired persons and households

A retired person is defined as anyone who describes themselves in the Living Costs and Food Survey (LCF) as "retired" or anyone over minimum National Insurance pension age describing themselves as "unoccupied" or "sick or injured but not intending to seek work". A retired household is defined as one where the combined income of retired members amounts to at least half the total gross income of the household.

6 . Data sources and quality

Household prices

While the calculation of inflation rates for household groups is straightforward analytically, data constraints make their estimation challenging in practice. An analysis of household group-specific inflation rates would ideally use price indices and expenditure weights specific to each household group. This would reflect the fact that different households will purchase goods and services from different outlets and, therefore, face different prices.

However, such data are not available and, therefore, we have had to use national price indices as an approximation. There are also challenges that arise from the data sources that we have available for us to calculate the expenditure shares. These limitations do not impede the validity of the chosen methodology and its robustness. For more information, please see our Methodology to calculate CPIH-consistent inflation rates for UK household groups.

Further information on strengths, limitations, appropriate uses, and how the data were created is available in our Household Costs Indices for UK household groups QMI.

7 . Related links

[Household Costs Indices for UK household groups](#)
Bulletin | Released 26 February 2024
Household Costs Indices, 12-month growth rates, expenditure shares and contributions for UK household groups and all-households.

[How increases in housing costs impact households](#)
Web page | Released 9 January 2023
Mortgage interest rates started to increase during 2022, this is likely to make borrowing more expensive for those with fixed rates deals coming to an end in 2023. Those with variable rate mortgages and private renters are also facing higher housing costs.

[Measuring changing prices and costs for consumers and households](#)
Article| Released 4 December 2023
Description of the different measures and approaches to inflation in the UK: Consumer Prices Index including owner occupiers' household costs (CPIH) and Consumer Prices Index (CPI), Household Costs Indices (HCIs) and Retail Prices Index (RPI).

[Household expenditure data insights into the effects of costs-of-living pressures](#)
Bulletin| Released 4 December 2023
Insights into the impacts of a period of price increases and cost-of-living pressures, and behavioural response of consumers, using household expenditure data.

[Consumer price inflation, UK](#)
Bulletin| Released 14 February 2024
Price indices, percentage changes, and weights for the different measures of consumer price inflation.

[UK House Price Index](#)
Bulletin| Released 14 February 2024
Monthly house price inflation in the UK, calculated using data from HM Land Registry, Registers of Scotland, and Land and Property Services Northern Ireland.

[Shopping prices comparison tool](#)
Web page| Released 3 May 2023
Search to see how the average prices of hundreds of shopping items are changing.

[How is inflation affecting your household costs?](#)
Web page | Released 23 March 2022
Use our inflation calculator to see how increases in the cost of living have affected you in the past year.

[Consumer Prices Indices Technical Manual, 2019](#)
Methodology | Last revised 22 March 2023
This technical manual is a reference tool for anyone wanting to understand how measures of consumer price inflation and associated indices are compiled.

8 . Cite this article

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