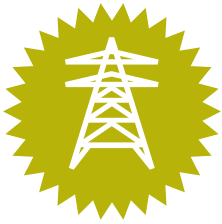


green alliance...

The great resource price shock

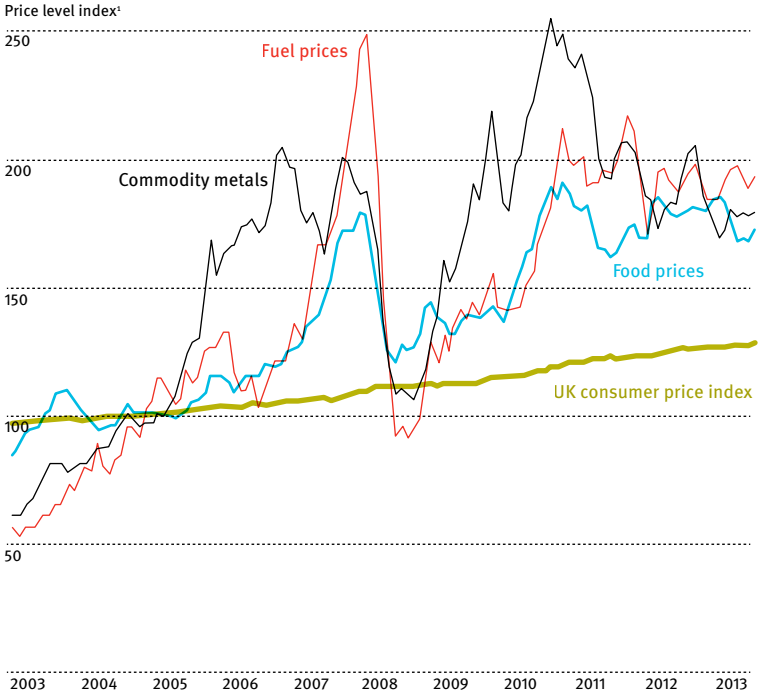
Over the past decade, world prices of key resources have risen sharply. This has meant that the cost of food and energy to UK households has gone up much more quickly than other household costs. If resource prices had just kept pace with other consumer prices, the average household could have saved over £1,000 on its food and household energy bills in 2012.

As the UK becomes more and more dependent on imports, rising resource prices will hurt the economy more and the poorest will continue to be the hardest hit. If this trend continues, by 2020 household food and energy bills could have risen by another £1,675 over and above general inflation.

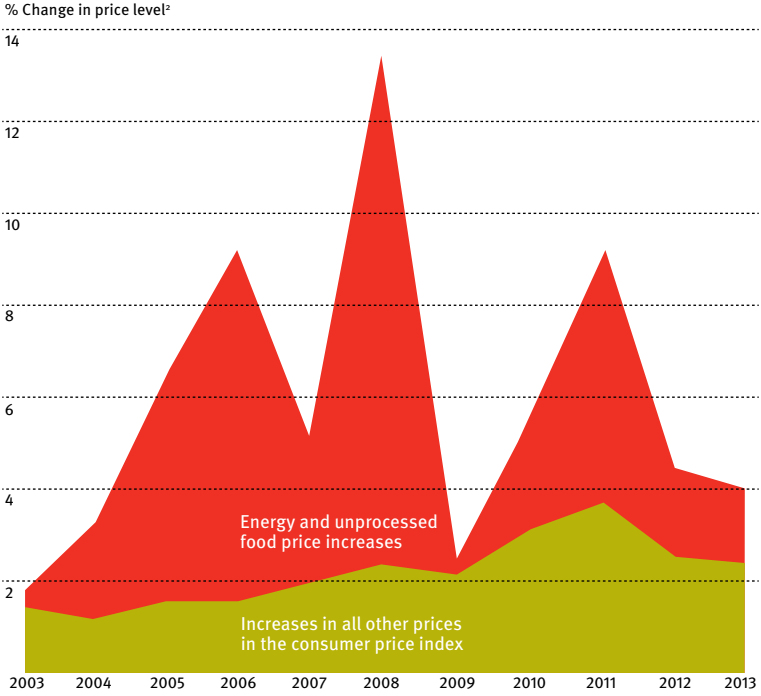
The only reliable way to protect the UK economy against these resource price shocks in future is to improve radically the efficiency of our resource use and reuse, reducing dependency on foreign imports. And if more countries did the same, increases in global demand would be reduced, helping to keep a lid on world resource prices.

The great resource price shock

World resource prices have surged ahead of UK consumer prices

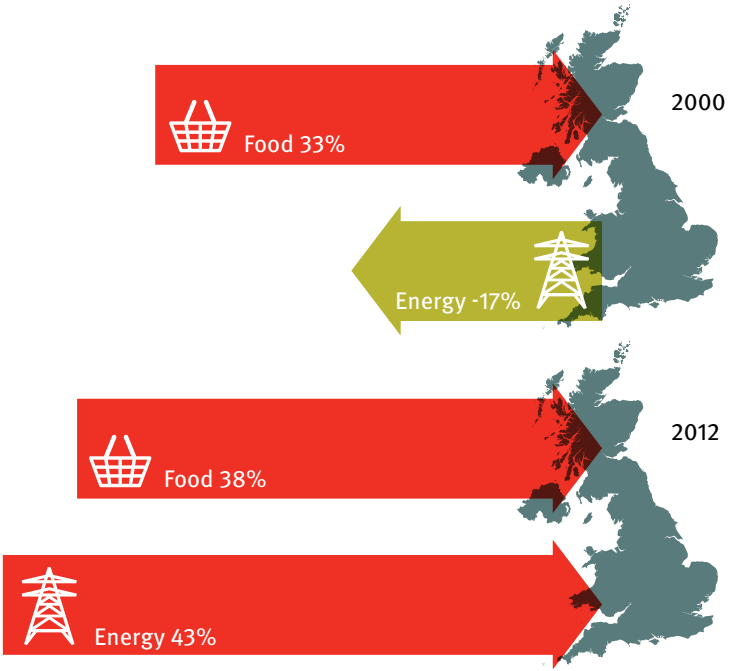


...so prices paid by UK households for food and energy have been going up faster than the cost of other items



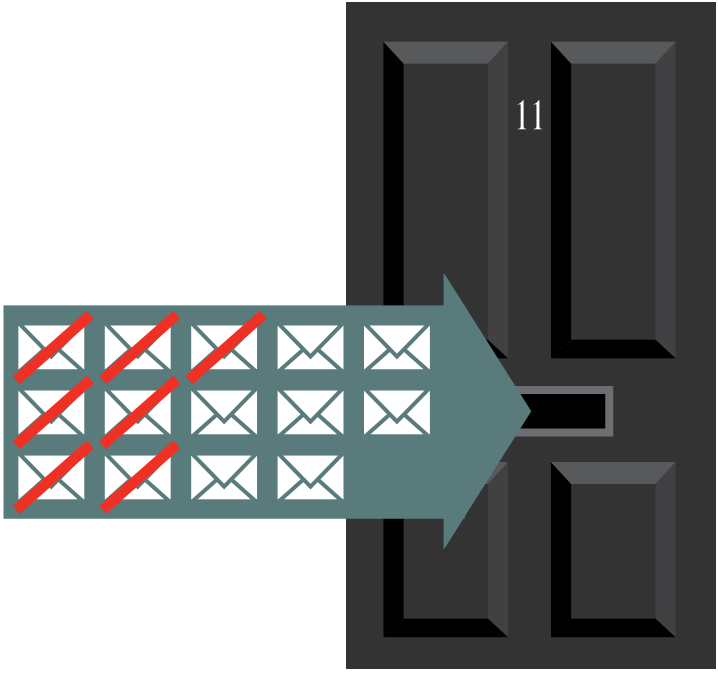
The UK is becoming more dependent on imports of food and energy, so world prices are hurting the economy more

Net import dependency[3]



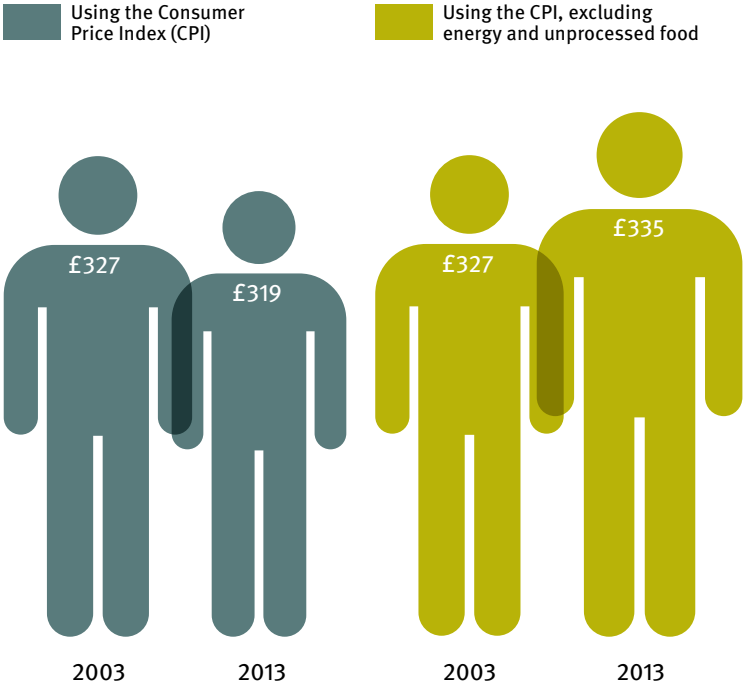
What if the great resource price shock hadn't happened?

At least half the letters written by the governor of the Bank of England to the chancellor of the exchequer since 2003, to explain overshooting inflation, may not have been necessary[4]



Wage increases may not have lagged behind inflation...

Real median weekly earnings at 2003 prices[5]



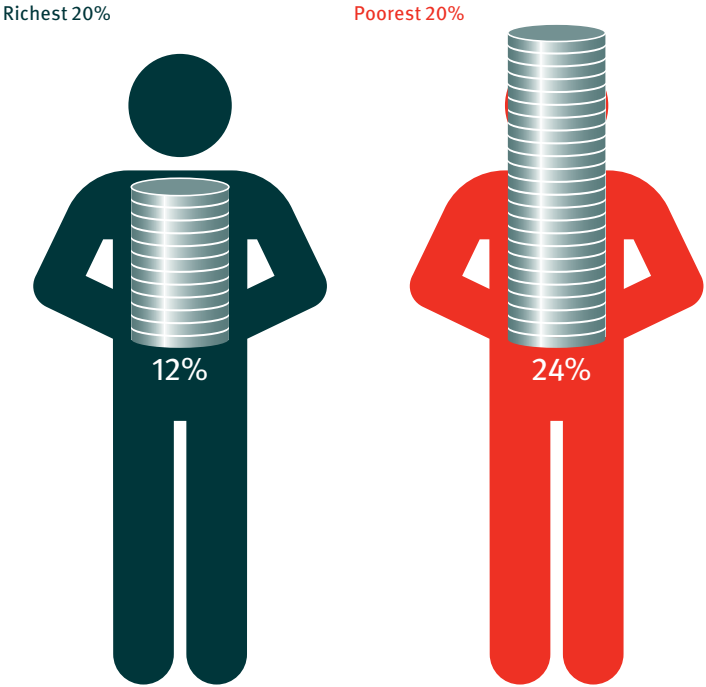
...and the cost of living should have been lower...

Average cost per household in 2012[6]

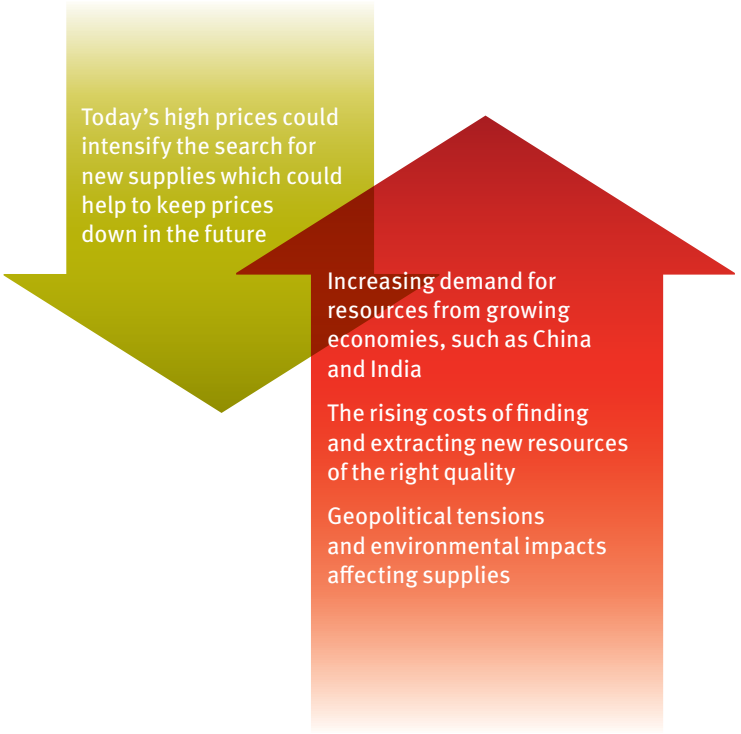
What it would have cost to buy this if food and energy prices had behaved like other prices since 2003[7]

...particularly for the poorest, who spend a higher proportion on food and domestic fuel

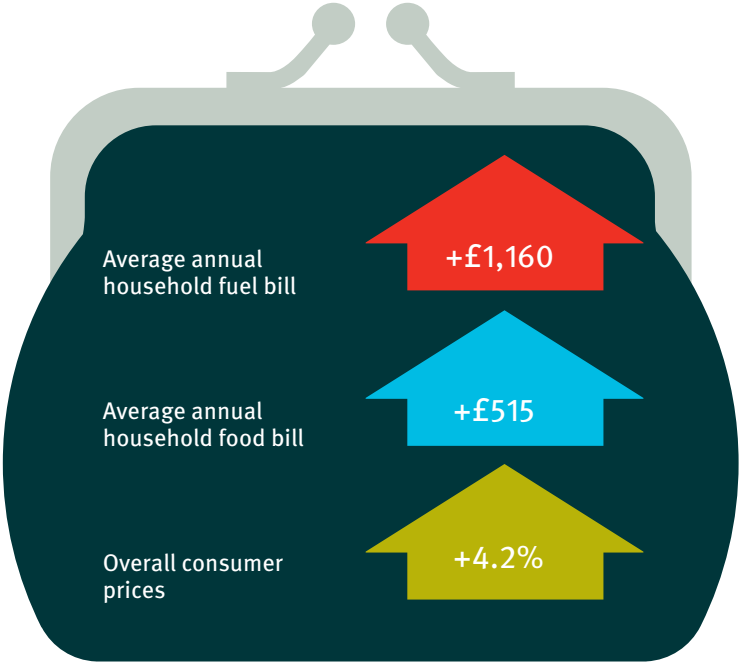
Proportion of household spending on food and domestic fuel[8]



What could drive resource prices in the future?



What could happen if current price trends continued to 2020?[9]



What are the options to protect the UK against this risk?

Hope for the best

Trust that new accessible and secure supplies are discovered to offset rising demand and that these supplies are not disrupted by geopolitics or environmental impacts.

This leaves the UK vulnerable to shocks

Resource nationalism

Try to secure resources abroad, such as agricultural land and energy sources, for UK use. Hope that foreign governments allow these agreements to be enforced in times of crisis.

This could promote conflict and is unreliable

Resource stewardship

Improve how efficiently resources are used and reused, to lower dependency on foreign imports. Encourage other countries to do the same to lower global demand and resource prices.

This is the only robust solution

Sources

[1] IMF, *Commodity Price Indices*; ONS, *Consumer Price Index* (CPI). All prices expressed as indices where 2005=100.

[2] ONS, CPI data showing year-on-year change for: Energy & unprocessed food (DKD7) and CPI, excluding energy and unprocessed food (DKC7)

[3] Energy (net import dependency ratio): DECC, 2012, *Energy trends;* and DECC, 2012, *UK energy in brief*; Food (approximation of net import dependency ratio, using inverse of food production to supply ratio): Defra, *Food statistics pocket handbook 2013*

[4] Fourteen letters were written between 2007 and 2012 to explain inflation breaches of more than one percentage point of the Bank of England's target of two per cent CPI inflation. If the threshold triggering letters had been expressed in terms of 'CPI, excluding energy and unprocessed food', only seven letters would have been sent. This only takes account of the direct effects of fuel and unprocessed food prices. If indirect effects of the prices of processed food and commodities, such as metals, minerals and plastics used in consumer goods, were removed it is likely even fewer letters would have been sent.

[5] ONS, *Median gross weekly earnings, all employees, table 4, Annual survey of hours and earnings*. Data spliced in 2004, 2006 and 2011 to account for breaks and provide a consistent series. Divided by CPI and CPI, excluding energy and unprocessed food (both rebased to 2003=100).

[6] ONS, *Family spending survey*. Using actual weekly spending in 2012 on electricity, gas and other fuels (not transport), and food & non-alcoholic drinks, multiplied by 52.

[7] Alternative spending on food and fuel calculated by rebasing 2012 spending to 2003 fuel and food prices using the electricity, gas and other fuels (D7CH) and food & non-alcoholic beverages (D7BU) sub-indices of the CPI and rebasing to 2012 in line with increases in the CPI, excluding energy and unprocessed food.

[8] ONS, *Family spending survey*. Share of weekly spending on electricity, gas and other fuels (not-transport) and food & non-alcoholic drinks, divided by total weekly spending. The poorest are the lowest income quintile (combining the lowest two deciles), whilst the richest are the highest income quintile (combining the top two deciles).

[9] Food and fuel: actual spending in 2012 projected forward to 2020, assuming that prices increase in line with the average increase in the electricity, gas and other fuels (D7CH) and food & non-alcoholic beverages (D7BU) sub-indices of the CPI, between 2003-12, and the average increase in the CPI, excluding energy & unprocessed food between 2003 and 2012. The increase in costs is the difference. Overall consumer prices: additional difference calculated by projecting forward to 2020 the average annual increase between 2003 and 2012 in the CPI and the CPI, excluding energy and unprocessed food.

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