

How Does an Individual's Inflation Experience Compare to the CPI

Comparing the CPI to an Individual's Inflation Experience

The Consumer Price Index (CPI) is a measure of the average change in prices paid by urban consumers for a market basket of goods and services.

Because the CPI is a statistical average, it may not reflect your experience or that of specific families or individuals, particularly those whose expenditure patterns differ substantially from the "average" urban consumer.

Because it is not practical to obtain prices for all consumer transactions in the United States, the CPI uses a carefully designed set of samples to estimate prices. These samples are the product of accepted statistical procedures to make the CPI representative of the prices paid for all goods and services purchased by urban consumers. Some of these samples include selected:

- Urban areas from all U.S. urban areas,
- Households within urban areas,
- Retail establishments from which these households (consumers) purchased goods and services,
- Specified and unique items--goods and services purchased by these consumers, Housing units from the urban areas for the shelter component of the CPI.

Therefore, the CPI is an average based on many diverse households and not a reflection of any particular household.

While several factors can result in the national CPI being different from your price experience, one major factor is how you actually spend your money.

Estimates of expenditures reported in the Consumer Expenditure Survey for each consumer good or service are used to produce "expenditure weights" for the CPI. These weights give each good or service in the CPI an importance relative to all the other goods and services in the market basket. For example, an increase of 5 percent in housing costs is more important than the same increase for telephone charges, because most consumers spend more for housing than for telephone service. Similarly, if you spend more than the average person on medical care and recreation, and prices rise sharply for these goods and services, the increase in your personal expenditures and personal price index would be larger than the increase for the average consumer. Because the CPI is a comprehensive measure, it contains items that are included in some individuals' buying patterns and excluded from others. For example, if you are a

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homeowner, you are more likely to buy major appliances such as refrigerators and laundry equipment than a renter would be.

The CPI divides the consumer market basket into eight major groups of goods and services. You can estimate the approximate difference in your expenditure pattern by estimating your relative expenditures for major groups of consumer goods and services. You could then compare them to the CPI groups' relative importance data, which are approximately the weights used in CPI estimation. For example, the approximate weights for the eight major groups in the CPI for All Urban Consumers (CPI-U) are listed below under the CPI-U average column. If your expenditure pattern is sharply different from the CPI average, the same price changes for the same expenditure categories would result in different price change measures for the total market basket. An example of a hypothetical expenditure pattern for a consumer with high expenditures for medical care appears in the tabulation that follows.

<u>Expenditure category</u>	<u>Percent Relative Importance (RI)</u>	
	Average (Dec.2001) (percent)	Hypothetical individual (percent)
Total (All Items)	100.0	100.0
Food and beverages	15.7	20.5
Housing	40.9	25.0
Apparel	4.4	4.5
Transportation	17.1	13.5
Medical care	5.8	25.0
Recreation	6.0	4.0
Education and communication	5.8	3.0
Other goods and services	4.3	4.5

Assume a price increase of 5 % for food and beverages and a 10 % increase for medical care costs, with no price changes for the other expenditure categories. This would result in a price index increase in the published CPI of 1.4 %. However, it would result in an increase of 3.5 % for the hypothetical individual's price index.

The area in which you live also can affect your price experiences. You should not expect the national or a regional CPI to always mirror your price experiences. It is possible, for example, that sharp price increases in one area are offset by lower prices in other areas, resulting in a more moderate price change published for the nation or a region.

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Another factor in whether you think the CPI reflects your price experience is that most consumers notice price changes in those goods and services purchased frequently. These items, such as food, clothing, and gasoline, have relatively large price swings because of the seasonal influences in supply and demand. Less attention is paid to many items (such as most household appliances) that are purchased infrequently, which often have relatively stable prices.

The CPI is used extensively to adjust incomes, lease payments, retirement benefits, food stamp and school lunch benefits, alimony, and tax brackets. The CPI, because of the many ways in which it is used, affects nearly all Americans. Because the CPI is based on the buying habits of the "average" consumer, it may not be a perfect reflection of your individual price experience. However, the CPI is the most economically feasible method for providing a statistic that is the most useful in all its applications.

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