

CONCEPT: CONSUMER PRICE INDEX (CPI)

- **Consumer Price Index (CPI)** – measure of the average change in prices of a typical family's “basket of goods”

□ Step 1: The government surveys households to see what kind of goods are typically purchased → the “basket”

A typical family in Simple Land purchases these items during a given year: 50 jugs of Water™ and 75 pounds of Food™

□ Step 2: The prices of the goods in the “basket” are determined

Year	Price of Water™	Price of Food™
2017	\$5	\$20
2018	\$5.05	\$22
2019	\$5.20	\$25

□ Step 3: The total cost of the “basket” is computed

2017 Cost of Basket =

2018 Cost of Basket =

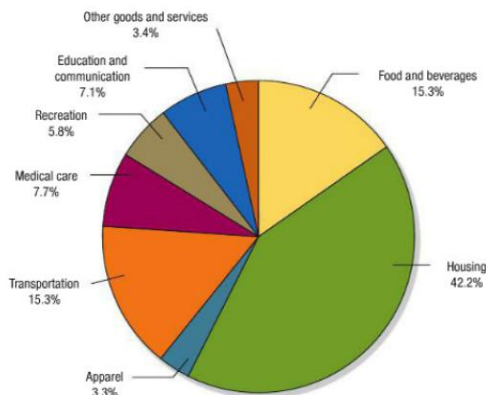
2019 Cost of Basket =

□ Step 4: The cost of the “basket” is compared to the chosen base-year → CPI is calculated

Formula	CPI for 2017	CPI for 2018	CPI for 2019
$CPI_{CY} = \frac{Basket\ Cost_{CY}}{Basket\ Cost_{BY}} * 100$			

□ Step 5: The CPI is used to calculate inflation rate (changes in prices over time)

Formula	Inflation for 2017	Inflation for 2018	Inflation for 2019
$Inflation_{CY} = \frac{CPI_{CY} - CPI_{PY}}{CPI_{PY}} * 100$			



The typical family's spending habits used to construct the “basket of goods” comes from a government survey of 14,000 households.

Source: U.S. Bureau of Labor Statistics