

Module 15 The Measurement and Calculation of Inflation

Discussion:

In September 2008, a tank of gas for a car cost \$58.40 (average price in the United States for regular gas, average size gas tank). In September 2007, the cost was \$43.84. The average size gas tank didn't change over that time-so why does it cost more to fill the tank?

Numerical Example: Calculating the Cost of a Market Basket

| | Pre-frost | Post-frost |
|--|-----------|------------|
| Price of orange | \$0.20 | \$0.40 |
| Price of grapefruit | \$0.60 | \$1.00 |
| Price of lemon | \$0.25 | \$0.45 |
| Cost of market basket (200 oranges, 50 grapefruit, 100 lemons) | \$95.00 | \$175.00 |

Discussion Questions:

- 1.) What does it mean to index a payment to the CPI and why is it done?
- 2.) What are examples of important payments indexed to the CPI?

Class Activity: Determine the most appropriate price index to use in each of the following situations and provide justification for each answer.

- 1.) Chris is writing a research paper on the automobile industry. She needs to include a discussion of how higher costs of production have affected American auto producers. What price index should she use?
- 2.) Charles works as an economist for the United Mine Workers. He is developing the justification for the pay raise the union is seeking from management in its new contract. What price index should he use?
- 3.) William is a television reporter. He is preparing a documentary on the status of the U.S. economy. His documentary will focus on all sectors of the economy. What price index should he use?
- 4.) In November, Lucy volunteered to compute the value of her grandmother's Social Security payments for the following year. What price index should she use?

