

Summary

- The cost of living index is also known as the consumer price index numbers. These are generally intended to represent the average change over time in the prices paid by the ultimate consumer of a specified basket of goods and services.
- The need for constructing consumer price indices arises because the general index numbers fail to give an exact idea of the effect of the change in the general price level on the cost of living of different classes of people, since a given change in the level of prices affects different classes of people in different manners. Different classes of people consume different types of commodities and even these same type of commodities are not consumed in the same proportion by different classes of people.
- The consumer price index helps us in determining the effect of rise and fall in prices on different classes of consumers living in different areas. The construction of such an index is of great significance because very often the demand for a higher wage is based on the cost of living index and the wages and salaries in most countries are adjusted in accordance with the consumer price index.
- It should be carefully noted that the cost of living index does not measure the actual cost of living nor the fluctuations in the cost of living due to causes other than the change in the price level. Its object is to find out how much the consumers of a particular class have to pay more for a certain basket full of goods and services in a given period compared to the base period. The term 'cost of living index' is used as consumer price index and retail price index in different countries with practically no difference in their connotation.
- It should be clearly understood at the very outset that two different indices representing two different geographical areas cannot be used to compare actual living costs of the two areas.
- A higher index for one area than for another with the same period is no indication that living costs are higher in the one than in the other. All it means is that as compared with the base periods, prices have risen in one area than in another. However, an actual cost depends not only on the rise in prices as compared with the base period, but also on the actual cost of living for the base period, which will vary for different regions and for different class of population.