Gdp vs cpi essays examples

Law, Security

GDP and CPI

Answer 1)

In economics literature, the term nominal refers to an unadjusted rate or value. In other words, the nominal value rate or value reflects the current situation such as current level of food prices without making any adjustment to inflationary levels or other associated factors. On the other hand, the term real measures the adjusted nominal value so as to present a more accurate representation of the economic value by removing the effects of general price levels over time. Below is the relationship between real and nominal values:

Rreal = RNominal – E(Inflation)

In most of the case of economic data representation, value or rates are always adjusted in real terms as real values are measures of purchasing power net of any price changes over time. For Example, Nominal GDP reflects the production quantities and prices in that time period, whereas the difference between real amounts in different time periods
reflect only changes in quantities.

Answer 2)

Consumer price index is an economic measure for calculating inflation from the weighted averages of prices of basket of goods and services. However, apart from regular CPI, even Chained CPI is the two popular economic tolls for measurement of inflation. In current era, Chained CPI is considered to be the accurate alternative than the regular CPI as the latter only measures periodic changes in price level of fixed basket of goods and services and does not consider any other relevant factor in measuring inflation in the economy. As a result, fixed weighted CPI usually carries number of disadvantages as overstatement of inflation by ignoring the disinflationary effect of quality improvements and new technology, in addition to the substitution effect.

On the other hand, Chained CPI, which is considered to be an accurate economic tool for measuring inflation, considers factors as product substitution made by consumers and other changes in their spending habits while measuring inflation. In this way an accurate measurement of inflation is made as rather than merely measuring periodic changes in the price of a fixed basket of goods, it (Chained CPI) accounts for the fact that consumers' purchasing decisions change along with changes in prices. Thus, with number of advantages associated with Chained CPI, US Bureau of Labor Statistics has started using Chained CPI for measuring inflation in the economy.

Which index leads to lower social security payments?

Since, Chained CPI Index measures the cost of living differently from the regular CPI Index by considering factors as product substitution etc, it leads to lower social security payments as cost of living will be lower with the chained CPI than the regular CPI. According to an estimate, under the chained CPI, cost of living adjustment will be 0. 3% less than the regular CPI. Although the 0. 3% difference does not seem large enough, but important to note that it keeps compounding over time. For Instance, if cost of living adjustment for the current year with regular CPI is 1. 7%, and if the monthly social security check received was $1250 last year, this will increase to

$1271. 25 with current year CPI. However, incorporating the effect of chained CPI, the retiree will get $3. 75 less per month or $45 less for the year. Again, that might not seem like a big reduction, but if the Cost of living adjustment is similar for next year also, the difference will increase to $7. 61 a month and $91. 32 for the whole year.

Thus, with Chained CPI leading to lower social security paychecks, the retirees will lose and the Federal Government will gain as their liability is reduced by the difference offered by regular CPI and chained CPI in cost of living adjustment.