Factors affecting standard of living

Economics

A higher National Income figure is required to maintain a high cost of living. Therefore, if the cost of living is higher in country B, the standard of living cannot be three times higher. The cost of living is determined by the amount of money needed to buy the goods and services necessary to maintain a specific standard of living. “ In 1890, the Bureau of Labor Statistics made the first attempt to gather data on the cost of living in the United States, introducing the cost-of-living index. In 1944 the government changed the name of its measurement from the " cost-of-living index" to the " consumer price index" (CPI), when a presidential committee made a comprehensive study and concluded that the cost-of-living index did not reflect all changes in living costs.” (US History Encyclopedia, 2010).

The difference in currency can also affect the cost of living in different countries. “ Data on relative standards of living is normally adjusted to reflect estimates of purchasing power parity to take account of differences in the cost of living – so that each unit of currency has approximately the same purchasing power.” (WorkGateways, 2010). In Europe, one Euro of income in each country may not have the same real purchasing power because of differences in the average cost of living. For example, relative prices of a basket of goods and services for consumers in Britain are estimated to be 18% higher than the European Union 15 average in year 2003.

Different geographical conditions can cause the standard of living to differ due to different climates. An example would be of the population in Europe that would have to spend on goods such as food and thick clothing to keep themselves warm during winter. During summer, they would have to spend on an entire different wardrobe to keep themselves cool. This lowers their annual income available for the consumption of other commodities. Whereas people in Asian countries such as Malaysia and Indonesia live under the same climate throughout the year. This enables them to survive with the same clothes for a longer period of time. In return, this increases the income available for the consumption of other goods and services.

Standards of living may even vary within the same country but in different states. For example in the United States of America, “ incomes of families in the Midwest and, especially, the South have tended to be lower than those of families in the Northeast and Far West. This reflects the concentration of farming, traditionally a low-income industry, in the former regions.” (US History Encyclopedia, 2010).

A difference in price levels does not reflect the standard of living. This is because the standard of living does not depend on the National Income figure but on real Income of the population. The National Income figure is higher in country B. This is because the prices of consumer goods in the country are much higher. The National Incfome figure in country A is lower because prices of consumer goods in Country A are lower. According to Eurostat, price levels in Europe for consumer goods and services in the year of 2008 differed widely across the continent.

In Denmark, consumer prices were 41% higher than the European Union Average, while in the former Yugoslav Republic of Macedonia, prices were 53% lower. If the price level index is higher than 100, the country concerned may be considered to be relatively expensive compared to the EU average, while if the price level index is lower than 100, then the country is relatively cheap compared to the EU average. “ An understanding of the differences in price levels is important in the comparison of economic data, such as gross domestic product, because higher relative prices could make an economy look healthier than it really is.” (Eurostat, 2010).

In certain countries such as Africa and Indonesia, non-monetary exchanges still occur to a large extent as compared to developed countries such as the United States of America. Monetary exchanges are included in the calculation of the national income while non-monetary exchanges are excluded. Non-monetary exchanges are “ methods of handling an exchange between one business entity and another that results in the acquisition of assets or services or the satisfaction of liabilities by surrendering cash assets or services or issuing other obligations.” (Accounting Dictionary, 2010). In a developed country, purchasing power is much higher as majority of the population has an annual income and is able to purchase goods and services to satisfy their needs and wants. This will reflect in a higher national income figure, thus, a higher standard of living. The need of non-monetary exchanges is low since citizens are able to survive on their income.

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