

NAME(S) \_\_\_\_\_

**PRINCIPLES OF MACROECONOMICS**

Economics 105 / Section 4 / Binder

**ASSIGNMENT #2: THE CONSUMER PRICE INDEX (CPI)**

*Due, with Weekly Work Record, on Sept. 18*

1. A Consumer Expenditure Survey in the city of Firestorm shows that people consume only firecrackers and bandages. In 1998, the year of the survey and also the reference base year, the average household bought 50 boxes of firecrackers at \$2 per box and 10 packs of bandages at \$1 per pack. In 1999, the price of firecrackers rose to \$2.25 per box and bandages rose to \$1.50 per pack. In 2000, the price of firecrackers was \$2.30 per box and the price of bandages was \$1.75 per pack.

What is the CPI basket? \_\_\_\_\_ boxes of firecrackers and \_\_\_\_\_ packs of bandages

What is the CPI in each year? 1998 \_\_\_\_\_

1999 \_\_\_\_\_

2000 \_\_\_\_\_

What was the inflation rate in 1999 and 2000?

1999 \_\_\_\_\_

2000 \_\_\_\_\_

Show all calculations for full credit.

2. Using the Consumer Price Index provided on the back of this sheet, adjust each of the following 1947 prices for the effects of inflation (that is, calculate the 1947 price in 1997 dollars). Show your calculations. Note any surprises with the 1947-to-1997 price comparison.

ITEM	1947 price	1997 price	1947 price, in 1997 dollars
University of Iowa tuition	\$130	\$2,470	
Gallon of gasoline	\$0.23	\$1.22	
3 minute phone call from NYC to LA	\$2.50	\$.045	
One day hospital stay in intensive care unit	\$35	\$2,300	
McDonalds hamburger	\$0.15	\$0.59	

Surprises?

NAMES \_\_\_\_\_

Hand this in as part of your assignment for this week (due Sept. 18).

**PRICES PROJECT**

For this project, you will develop a Student Price Index, based on items that are most consumed by students. For now, select a basket and find the prices for each item in your basket. You should have between 8 and 10 items in your basket. Select quantities based on how much is purchased in one month. Later in November I will ask you to re-price your basket, calculate the CPI and inflation rate, and consider the issues involved in constructing a useful index. Take care in constructing your basket, as the prices project is worth 100 points. This part of the project is worth 25 points.

ITEM	QUANTITY	PRICE	Source of price data (store or business from which you got the price)

Total cost of your basket: \_\_\_\_\_

On the reverse side of this sheet, justify your choice of a basket (both items and quantities). Why did you choose the items and quantities you did? How does your student price index differ from the CPI? Why might it be a better reflection of the cost of living for students than is the CPI? Does this mean there is more than one inflation rate?