

Understanding the Consumer Price Index

Kevin Dolan, September 2024

On Tuesday, September 17, Statistics Canada is expected to indicate that the **August reading for Canadian Inflation** fell to 2.4% from the July 2.5% and a decline will allow the Bank of Canada to continue its path for lower Interest Rates. Inflation is measured using **the Consumer Price Index (CPI)** which shows the rate of price change for goods and services bought by Canadian consumers.

The Canadian CPI began with a study conducted by the Department of Labour in the early 1900s. The study was based on a hypothetical family budget that represented weekly expenditures of an urban working-class family of five.

The CPI is defined, more precisely, as an indicator of the changes in consumer prices experienced by Canadians. It is obtained by comparing, through time, **the cost of a fixed basket of commodities** purchased by Canadian consumers in a particular year. Since the basket contains commodities of unchanging or equivalent quantity and quality, the index reflects only pure price movements.

The CPI is not a cost-of-living index, though people frequently call it this. In theory, the objective behind a cost-of-living index is to measure price changes experienced by consumers in maintaining a constant standard of living. The idea is that consumers would normally switch between products as the price relationship of goods changes.

Every month, the news media report the CPI figures to the Canadian public. Some people question these figures because their personal experience does not seem to match what is being reported. It is important, however, to understand that the CPI **measures the average change in retail prices encountered by all consumers** in Canada. It cannot, and should not, be expected to reflect the price change experience of any particular household or person. The CPI basket contains an extensive list of goods and services.

The goods and services in the CPI basket are divided into **8 major components**: Food; Shelter; Household operations, furnishings and equipment; Clothing and footwear; Transportation; Health and personal care; Recreation, education and reading, and Alcoholic beverages, tobacco products and recreational cannabis.

