**Measuring Inflation**

This is done to gather what prices businesses are setting in the UK currently and so an **average** can be found

Price Surveys are conducted in the UK

This allows a price index to be calculated of the average price level in the UK, weighted by the amount spent on each good.

A family expenditure survey is conducted annually

This tells us how much people are spending on different goods so they can be **weighted** according to their importance

Inflation is measured by trying to calculate **how much** **on average a representative a basket of goods and services costs in the UK.**

In order to do this there are several steps:

**1. Price Surveys:**

**2. Annual Family Expenditure Survey:**

**3.** All this information is then used to construct a **weighted price index**. An index number is usually started in a base year at a value of 100. The number itself has no meaning and has no units, it is the changes in the number that are important.

**4.** If the price index figure rises we have **inflation**. However, if it falls we have **deflation**.

**Limitations with Inflation Measurement**

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| **Limitation** | **Explanation** |
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 **Inflation and Index Numbers**

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Activity 1: Calculating Inflation Using Index Numbers



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| --- | --- | --- |
|  | **YEAR 1** | **YEAR 2** |
| **Item** | **Price**  | **Index** | **Weight(out of 10)** | **Weighted Index**  | **Price**  | **Weight (out of 10)** | **Index(1dp)** | **Weighted Index (1dp)** |
| **Bread** | £1.05 | 100 | 3 | 300 | £1.10 | 3 | 104.8 | 314.4 |
| **Cheese** | £2.10 | 100 | 3 | 300 | £2.20 | 3 | 104.8 | 314.4 |
| **Cornflakes** | £1.20 | 100 | 0.5 | 50 | £1.20 | 0.5 | 100 | 50 |
| **Bananas** | £0.20 | 100 | 0.5 | 50 | £0.25 | 0.5 | 125 | 62.5 |
| **Netflix** | £5.99 | 100 | 1 | 100 | £5.00 | 2 | 83.5 | 167 |
| **Cinema Tickets** | £8.00 | 100 | 2 | 200 | £7.50 | 1 | 93.8 | 93.8 |

**Average weighted index Yr 1 =**

1002.1 / 10 = **100.2**

**Average weighted index Yr 1:**

1000 / 10 = **100**

**Key Formulae:**

Index = current year x 10

base year

Average weighted index
= Sum of weighted indices
Total weights

**Inflation between year 1 and 2 =**

**Activity 2:**

**1. What survey would have been conducted to find the average price of bread?**

**2. What survey would have been conducted to include the weightings? Why is it important to weight the index?**

**3. Why do you think the weightings changed for Netflix and cinema tickets? Why is this necessary?**

**4. An OAP spends no money on Netflix or cinema tickets but significantly more on bread, cheese and bananas.**

**a) Why is the inflation rate less accurate for their cost of living?**

**b) Will it be higher or lower for the OAP than on average?**

 **Different Measures of Inflation**

**Different Measures of Inflation
.**The two main measures of inflation are:

* Retail Price Index (RPI)
* Consumer Price Index (CPI)

**The Retail Price Index: RPI**

The RPI is a traditional measure of the price level and is used by trade unions to negotiate wages and by utility regulators to set prices. The Bank of England previously used to target RPI inflation at a rate of 2.5% ( + or – 1%).

**The Consumer Price Index: CPI**

CPI is a more recent measure of the price level, having been officially calculated from 1996. It is the EU measure and therefore allows comparisons to be made between EU countries. This is the main reason the Bank of England now uses it as its main measure of inflation; targeting CPI at 2% (+ or – 1%). However, the RPI will still continue to be calculated.

**Differences between CPI and RPI**

1. **CPI excludes a number of items RPI includes** **mainly relating to housing costs.** These include:

* Council tax
* Mortgage interest payments
* House depreciation
* Building insurance, estate agents and conveyancing fees

Therefore in times of housing boom the CPI will be lower than the RPI as housing costs rise at a faster rate than other items. However, with very low interest rates, mortgage repayments & housing costs the RPI figure were much lower than the CPI figure, such as in 2009.

2. **RPI excludes high income households (top 4%) and pensioners who derive at least 75% of their income from the state** whereas the CPI includes all households.

**Activity 3: The UKs Inflation Target**

1. **What is it?**
2. **Who is it set by (and why)?**
3. **Why is it set at this level?**

 **Employment & Unemployment**

**Defining Employment & Unemployment**

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| --- | --- |
| **Employment** | “the total number of people with a job” |
| **Unemployment**  | “people who are **able**, **available** and **willing** to work but cannot find a job despite an active search for work.” |

As you can see from the definition of unemployment, it is essential to know whether potential employees are available, willing and able to work at the current wage rate. Therefore we need to distinguish between different groups of people in the UK.

**UK Population:**

All the people living in the UK

However, some are the wrong age to work

**Population of working age:**

All the people living in the UK aged between 16 and 65.

**INACTIVE**

However, some are not willing and able to work

Some are willing and able to work

**Workforce**

All the people living in the UK aged between 16 and 65 who are willing and able to work

Some have a
job

Some do not
have a job

**EMPLOYED**

**UNEMPLOYED**

**The Level and Rate of Employment & Unemployment**

**a) Levels of Employment and Unemployment**

The level of employment is simply the **number of people** in work and the level of unemployment is the **number of people** who are willing and able to work but are not currently employed.



Although unemployment and employment can be measured at a point in time, the number of people gaining and losing jobs is constantly changing. Assuming a constant size of the UK workforce:

* **If more people are gaining jobs than losing jobs:** employment rises and unemployment falls
* **If more people are losing jobs than gaining jobs:** employment falls and unemployment rises

However the workforce may not be constant, if more people join the UK workforce:

* **If these people find a job:** it will boost employment
* **If these people cannot find a job:** it will boost unemployment

 **b) Will the levels of employment and unemployment always move in opposite directions?**

Although it would seem logical that more people being employed would reduce unemployment, this is not necessarily true and is again due to changes in activity and the labour force. For example, if 100 workers join the labour force and half gain a job then the level of employment and unemployment would rise.

**c) Rate of Employment and Unemployment**

According to the ONS the rate of unemployment was 5.5% at the end of March 2015

The rate of employment is = Numbers employed x 100

 UK Workforce

The rate of unemployment is = Numbers unemployed x 100

 UK Workforce

The rates of unemployment and employment therefore are **as a proportion of the current UK workforce**. Therefore the rate of unemployment and employment may change not only due to changes in the number of people gaining or losing jobs but also the size of the UK workforce. For example, if the Government deems many people previously counted as inactive (on incapacity benefits) as now able to work this will increase the size of the UK workforce. If these people do not get a job it could increase the rate of unemployment and reduces the rate of employment.

 **Measuring Unemployment**

**Measuring Unemployment**

|  |  |
| --- | --- |
| **Claimant Count Measure** | “The number of people claiming unemployment benefits. Claimants must be registered at the job centre, be over 18 (but not retired) and be actively seeking employment” |
| **ILO Measure** | “The number of people, aged 16-65, who have been out of work for 4 weeks and ready to start in 2 weeks. Based on the internationally recognised labour force survey” |

 **UK unemployment is measured in two main ways**

**Claimant Count**

**ILO**

**Measured:** ILO Survey (phone/interview) Numbers claiming JSA

**Age:** 16-65 18 – retirement (60/65)

**Qualification:** Out of work for 4 weeks Registered at the Job Centre

 Ready to start in 2 weeks Actively seeking employment

 Ready to start now

**Problems with the Measures**

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| --- | --- |
| **ILO Measure** | **Claimant Count** |
| **- Sampling Issues:** the ILO is only a sample of the population and this therefore limits its accuracy. The quality of the figures will therefore depend on the accuracy & reliability of the surveys.**- Out of date:** the ILO measure is 6 weeks out of date when it is published.  | **- Too open to Government manipulation**: in the 1980s and 1990s the Government introduced over 30 different changes, most of which reduced the unemployment figure.**- Not internationally recognisable** and therefore couldn’t be effectively used to make comparisons between countries.**- People may be unemployed but don’t claim:** e.g. due to the stigma attached |

**Differences between CC and ILO measures**

**The claimant count may be lower than the ILO because they are deemed unemployed on the ILO measure but are not claiming JSA, for example due to:**

* **Youth Unemployment is not included:** workers who are youth unemployed between the ages of 16 and 18 will could as unemployed on ILO due to the wider range of ages in the criteria. However, they cannot claim as they are not old enough to be eligible for JSA. This is exacerbated by more students trying to find part-time jobs (e.g. due to the higher tuition fees) and being unable to get jobs in a competitive job market (e.g. due to the economic downturn).
* **JSA may be hard(er) to obtain:** for example the current Government have made it harder to claim JSA and therefore, with less people eligible, the claimant count figure would fall but the ILO measure would be unaffected
* **Workers do not claim benefits even when entitled:** workers may be happy to respond to the ILO to say they are unemployed but not want to claim JSA due to the **stigma** attached to claiming benefits.
* **Other groups not entitled to JSA but will be counted as unemployed on ILO**.
e.g. female workers looking for work but not entitled to benefits due to living in a household where their partner is earning too high a wage to be entitled to JSA.

e.g. the elderly may be looking for work but are not entitled to benefits due to collecting pensions from their previous employer

**However, the CC may be higher than the ILO because:**

* **The CC may include some people not included in the ILO measure**

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e.g. may claim benefits for being unemployed but actually be in work, usually as self-employed.

 **Overall Limitations of Unemployment Measures**

May **underestimate** unemployment as they exclude:

1. Part­-time workers looking for full-time work

2. Those on Government training schemes who would prefer to be in work

3. People not actively seeking work or on benefits but would take a job if offered one.

4. Unemployed workers who have been taken off the unemployment register by moving them onto sickness and disability benefits.

May **overestimate** unemployment as they include:

1. People who will never be able to get a job and are unemployable are still counted (unless they become inactive).

e.g. with physical or mental disabilities, ex-criminals or with no formal qualifications.