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Developing a Consumer Price Index for the Elderly

Statement of
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Special Committee on Aging
United States Senate

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Mr. Chairman and Members of the Committee:

We are pleased to be here today to assist the Committee in its deliberations on developing a consumer price index (CPI) for the elderly.

From time to time, questions arise about whether movements in the general consumer price index accurately reflect trends in the prices paid by specific subgroups of the population. Several years ago, in response to such questions, GAO examined in detail the need for a special CPI for retirees.

In our 1982 report on that subject[1], we

-- explained in some detail how the CPI is constructed and which elements of the calculation could cause the index to misrepresent changes in the cost of living for retirees,

-- reviewed previous analyses of differences between inflation as measured by the general CPI and as measured by an index more representative of the buying patterns of retirees,

-- constructed several versions of an illustrative retirees' CPI and compared changes in them with changes in the general CPI, and

-- explored what steps might be needed to produce a special retirees' CPI of sufficient accuracy that it might be used to index benefit programs.

[1]"A CPI for Retirees Is Not Needed Now But Could Be in the Future" (GAO/GGD-82-41, June 1, 1982).

We reported that among the factors which could cause a retirees' CPI to differ from the general CPI were differences between the budgets of retirees and the budget reflected in the general CPI, differences in the geographic distribution of retirees versus the general population, and differences in the places where retirees shop compared to the general population. If retirees devote a greater proportion of their total expenditures to food, for example, than does the general population, changes in food prices would affect a retirees' CPI more than the general index. Likewise, if a greater proportion of retirees live in the Soutwest, for example, compared to the general population, a retirees' CPI would be affected more by price changes in that area of the country than would the general index. And finally, if retirees tend to frequent places of business other than those from which the Bureau of Labor Statistics (BLS) collects the prices used to compute the general CPI, that CPI might not reflect the price changes being experienced by retirees.

Most of the prior studies we reviewed focused on the elderly (generally defined in those studies as persons 65 years old or older) and involved the construction of indexes that had been reweighted to reflect more closely the budgets of the elderly. Those studies generally concluded that price increases as measured by those reweighted indexes were not substantially different from increases as measured by the general CPI.

Because we were interested in possible implications for adjusting federally-administered retirement programs, our 1982 report focused on retirees rather than the elderly. We identified someone as retired if BLS' data showed that the person (1) was at least 50 years old, (2) listed his or her occupation as retired, and (3) reported no earned income such as wages and salaries. By using unpublished BLS data, we were able to create hybrid retirees' indexes which adjusted more completely for differences in household budgets than did most of the other studies, which reflected spending patterns of persons who were retired (as opposed to those in a certain age group), and which, unlike the other studies, adjusted for some of the differences in the geographic location of retirees compared to the general population. We made our analyses using two different methods for measuring housing costs--the one BLS was using at the time of our study and the one it eventually implemented in 1983. We looked in particular at price changes from the first quarter of 1978 through the first quarter of 1981.

We found, after recognizing the change in BLS' measure of housing costs, that inflation as measured by the special retiree indexes we constructed did not differ significantly from inflation as measured by a general CPI. We found also that our adjustment for differences in geographic location did not alter this result significantly. There was insufficient information available, however, to enable us to determine whether retirees typically frequent different places of business than the general population and to what extent, if at all, that would affect our results.

We concluded that the evidence we had assembled did not, at that time, justify creating a special CPI for retirees of a quality similar to that of the general CPI. We also concluded, however, that at some future time price trends might well change sufficiently that a fully developed CPI for retirees would be justified. Thus, we recommended that the BLS compute an experimental retirees' index, at least annually, using the general methodology we had employed. This experimental index would use data currently available to BLS and would reflect the effect of differences in the composition of household budgets.

BLS disagreed with our recommendation. It felt that more information was needed as to where retirees shop, for example, before constructing a retirees' index. We agreed that more information would be needed before a retirees' CPI could be developed for use in computing cost of living adjustments. In particular, the consumer expenditure surveys used to derive household spending patterns might have to be expanded to obtain more accurate data on the particular spending patterns of retirees, and studies would have to be conducted to determine if differences in the places where retirees shop introduce additional differences in inflation patterns. However, we viewed the experimental index not as a vehicle for computing cost of living adjustments but as a relatively low-cost tool for monitoring the relationship between the general index and a possible retirees' index which could be used to judge whether the additional work and cost involved in creating a fully-developed retirees' CPI was justified. We continue to hold that view, while cautioning again that such an index should not be used for purposes other than monitoring unless and until further developmental work has been undertaken.

We should point out, in closing, that there is an index now being published by BLS that we think is more appropriate than the index being used to compute cost-of-living adjustments for federally administered retirement programs like social security. The index now used is the CPI-W, which measures the price changes associated with goods and services bought by urban wage earners and clerical workers. As we noted in our 1982 report, we believe the more appropriate index is the CPI-U because it measures the price changes associated with goods and services bought by all urban consumers, including the retired.

This concludes my prepared statement. I will be pleased to answer any questions you may have.