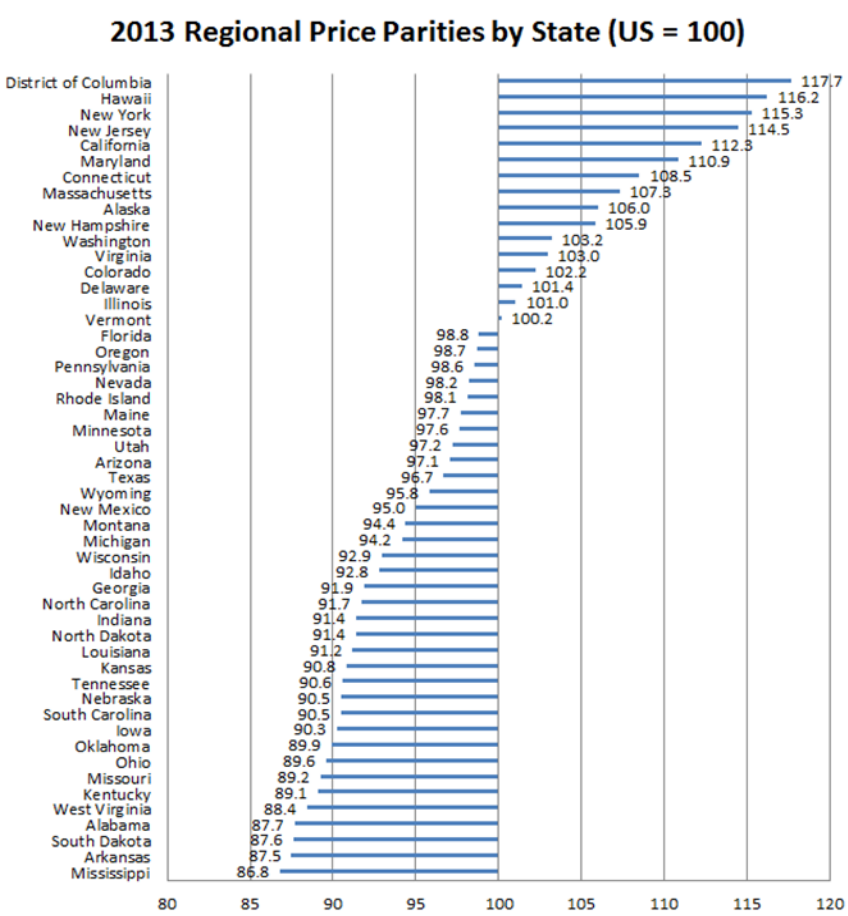
Regional Price Parities: Adjusting Wages for the Cost of Living

Scott Smith, Regional Economist

The dollar amount written on a paycheck is not the only determinate of the true value of wages. For one, the price of goods and services generally increases over time. The economic term for general price increases is inflation. If wages do not keep pace with inflation, the value of a paycheck shrinks.

Secondly, location matters when assessing the purchasing power of wages .The price of a product or service in one city may be different than the price for the same product or service in a different city. Prices differ because geographical scarcities and localized consumer preferences can dramatically impact supply and demand.

For example, most Americans spend a significant portion of their income on rent and mortgages. In densely populated areas, land is scarce relative to the number of people looking for housing. This drives up the price. Conversely, low density areas can more easily meet the housing needs of the population, which reduces the price of housing. The effects of geographical scarcity can be applied to every product and service in a local economy.



Source: Bureau of Economic Analysis.

The U.S. Bureau of Economic Analysis uses Regional Price Parities (RPPs) to account for the cost of living in specific locations. RPPs measure the differences in the price levels of goods and services across states and metropolitan areas for a given year. RPPs are expressed as a percentage of the overall national price level, where the national average equals 100. State and metropolitan RPPs can be accessed on the BEA website, and the accompanying chart shows the RPPs for each state in 2013. The 2013 RPP for Utah is 97.2, which means that average price levels in the state were 2.8 percent below the national average.

The data also allows for the examination of prices in metropolitan areas. The table below highlights the effects of regional price differences on median annual incomes for the five largest and smallest metropolitan areas in the U.S as well as the five Utah metropolitan areas (each metropolitan area has its own unique RPP which is different from the number shown on the state table).

Wages and RPP's by Metro Area *

	Median Wage	***RPP***	***Adjusted Wage***
New York-White Plains-Wayne, NY-NJ Metropolitan Division	*45,200*	*122.3*	*36,958*
Houston-Sugar Land-Baytown, TX	*36,880*	*100.6*	*36,660*
Salt Lake City, UT	*35,780*	*99.7*	*35,888*
Chicago-Joliet-Naperville, IL Metropolitan Division	*37,950*	*106.6*	*35,600*
Salisbury, MD	*31,370*	*89.8*	*34,933*
Ogden-Clearfield, UT	*33,120*	*95.9*	*34,536*
Mansfield, OH	*29,590*	*88*	*33,625*
Manhattan, KS	*30,970*	*92.8*	*33,373*
St. Joseph, MO-KS	*29,410*	*89.2*	*32,971*
Coeur d'Alene, ID	*30,440*	*92.8*	*32,802*
Los Angeles-Long Beach-Glendale, CA Metropolitan Division	*38,100*	*117.7*	*32,370*
Logan, UT-ID	*29,010*	*90.6*	*32,020*
Provo-Orem, UT	*31,100*	*97.3*	*31,963*
St. George, UT	*28,990*	*94.3*	*30,742*

Source: Bureau of Labor Statistics, Bureau of Economic Analysis
** - 2014 Wages and 2013 RPP's*

All the Utah areas have an RPP under 100, which means that a dollar in any of Utah's metros has more purchasing power than the national average. Utah's reasonable cost of living can be attributed to its relatively low housing costs, which were 7.1 percent below the national average.

The adjustments of the RPP reveal that the absolute values of Utah wages are undervalued because Utahans have greater purchasing power relative to national averages. Further, it needs to be noted that purchasing power is an imperfect measure of quality of life. Residents of rural areas have made a lifestyle choice that is often independent of money wages.