

Value Of Money

Uses of Index Numbers:

Index numbers can be used for a number of purposes:

(iii) We can also compare, with the help of index numbers, economic conditions of a class of people at two different periods.

(iv) Index numbers can be used as basis for, and equitable discharge of, contracts relating to borrowing and lending. We know when prices rise, creditors lose. It may perhaps be considered more just to ensure that the creditor gets back the same purchasing power. Hence, when prices rise, the debtor may be asked to pay a correspondingly higher sum to discharge a debt.

Limitations:

It may, however, be pointed out that index numbers are not a faultless guide.

They suffer from a number of limitations, some of which are given below:

(i) Approximations:

Index numbers are at best only approximations. They cannot be taken as infallible guides. Their data are open to question and they lead to different interpretations.

(ii) International Comparisons Difficult:

Use of index numbers for international comparisons presents several difficulties. The result is that such comparisons are difficult, if not impossible, on account of the different bases, different sets of commodities or differences in their quality, etc.

(iii) Comparisons between Different Times Difficult:

It is not easy to institute comparisons between different periods of time. Over long periods, some popular commodities are replaced by others. Entirely new commodities come to figure in consumption, or a commodity may be vastly

different from what' it used to be. Think of a modern railway engine and one of the early ones. Ford cat 1985 is a different commodity from the 1950 Ford.