

Cost of Living Definition

By [CAROLINE BANTON](#) Updated May 7, 2019

What Is the Cost of Living?

The cost of living is the amount of money needed to sustain a certain [standard of living](#) by affording basic expenses such as housing, food, taxes, and healthcare. The cost of living is often used to compare how expensive it is to live in one city versus another. The cost of living is tied to wages. If expenses are higher in a city, such as New York, for example, salary levels must be higher so that people can afford to live in that city.

Cost of Living and Lifestyle

The cost of living can be a significant factor in personal wealth accumulation because a salary can provide a higher [standard of living](#) in a city where daily expenses such as rent, food and entertainment are less. In contrast, a high salary can seem insufficient in an expensive city such as New York. In a 2018 survey, Mercer, a global human resources firm, finds the [cities with the highest cost of living](#) include Hong Kong; Luanda, the capital of Angola; Tokyo; Zurich and Singapore, in that order. New York City was ranked the [costliest city in the United States](#) followed by San Francisco and Los Angeles, Chicago, Washington and Boston.

The Cost of Living Index

The [cost of living index](#) compares the cost of living in a major city to a corresponding metropolitan area. The index incorporates the expense of various living expenses creating an aggregate measure that workforce entrants can use as a benchmark. As college graduates weigh employment alternatives and currently employed job seekers consider relocation, the index provides an informative snapshot of rental, transportation and grocery costs.

Different indexes may calculate living expenses differently. For example, in 2018, [Kiplinger](#) found San Diego to be the most expensive city based on the Council for Community and Economic Research, not New York City. The Council's cost of living index measured prices in 269 urban areas for expenses such as housing, groceries, utilities, transportation and healthcare, even getting a hair cut or going to a movie. In the case of San Diego, the cost of housing is 138% above the national average, and the cost of transportation is over 20% higher than the national average.

Fast Fact: Four out of five of the world's most expensive cities for expatriates are now in Asia.

Cost of Living and Wages

The rising cost of living has spurred debate over the [U.S. federal minimum wage](#) and the disparity between the lowest salary allowed by law and the earnings needed to maintain an adequate cost of living. Proponents of a hike in wages cite increased worker productivity levels

since 1968 as inequitably correlated to the minimum hourly rate of pay. As pay levels once tracked the increase in productivity, the divergence between earnings and worker efficiency has reached historically disproportionate levels. By contrast, opponents of a minimum wage contend that a raise could spur higher consumer prices as employers offset rising labor costs.

Fast Fact: Multinational corporations use cost of living to assess expatriate salary packages for international assignees.

Wage Increases and Cost-of-Living Adjustments (COLAs)

In 1973, Congress enacted legislation to address [cost-of-living adjustments](#) (COLAs). COLA adjustments for Social Security and Supplemental Security Income (SSI) benefits were instituted so that the payments keep pace with [inflation](#). For example, in December 2018, the COLA was 2.8% and the increased amounts were to be paid, starting in January 2019. Federal SSI payment levels increased by the same percentage.

The [Social Security Act](#) requires [COLAs](#) to be based on increases in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). The Social Security Administration states that:

A COLA effective for December of the current year is equal to the percentage increase (if any) in the CPI-W from the average for the third quarter of the current year to the average for the third quarter of the last year in which a COLA became effective.

KEY TAKEAWAYS

- Cost of living is the amount of money needed to sustain a certain standard of living by affording expenses such as housing, food, taxes, and healthcare.
- Salaries should reflect the higher cost of living in more expensive cities like New York City.
- The cost of living index compares the cost of living in a major city to a corresponding metropolitan area.

Real World Example

The Economic Policy Institute [updated](#) its [Family Budget Calculator](#) in March 2018. The calculator helps families determine how much salary they will need to cover the cost of living in 3,142 counties in all 611 metro areas.

The calculator finds San Francisco to be the most expensive city and a two-parent household with two children would need a total income of \$148,439 with a basic budget for expenses. The least expensive metro area was Brownsville, Texas where the same family would need a median income of \$32,203. Interestingly, there is nowhere in the United States where a single adult with no children would be able to cover the cost of living earning [the minimum wage](#).

Related Terms

[Cost of Labor Definition](#)

The cost of labor is the total of all employee wages plus the cost of benefits and payroll taxes paid by an employer. [more](#)

[Cost-of-Living Adjustment \(COLA\)](#)

A cost-of-living adjustment (COLA) is made to Social Security and Supplemental Security Income to adjust benefits to counteract the effects of inflation. [more](#)

[Personal Finance](#)

Personal finance is all about managing your income and your expenses, and saving and investing. Learn which educational resources can guide your planning and the personal characteristics that will help you make the best money-management decisions. [more](#)

[Gentrification Definition](#)

Gentrification refers to the transformation of a city neighborhood from low to high value, often leading to the displacement of its previous occupants. [more](#)

[S&P CoreLogic Case-Shiller National Home Price Index Definition](#)

The S&P CoreLogic Case-Shiller National Home Price Index measures the change in value of the U.S. residential housing market. [more](#)

[Consumer Price Index – CPI Definition](#)

The Consumer Price Index measures the average change in prices over time that consumers pay for a basket of goods and services. [more](#)