

Micro Economics

Sem – I

1.2.1 (a) Defects of Cardinal Utility Approach

Some of the major defects and weaknesses found in the Marshallian utility analysis are discussed below:

(1) Cardinal measurability of Utility is unrealistic:

The entire Marshallian utility analysis is based on the hypothesis that utility is cardinally measured. According to the cardinal approach, the utility of a commodity is measured in 'utils' or units and that can be added and subtracted. For example, when a consumer takes the first panipuri, he gets utility equivalent to 15 units; from the second and third panipuri 10 and 5 units respectively and when he consumes the fourth panipuri marginal utility becomes zero. If it is supposed that he has no desire after the fourth panipuri the utility from the fifth will be negative 5 units. In this way, the total utility in each case will be 15, 25, 30 and 30, when from the fifth panipuri the total utility will be 25 (30-5).

Hicks considers that the basis of the utility analysis that it is measurable is defective and unrealistic because utility is a subjective and psychological concept, which cannot be measured cardinally. In reality, it can be measured ordinarily.

(2) Single product Model is Unrealistic:

The utility analysis is a single commodity model. The utility of one commodity is regarded independent of the other. Marshall assumes substitutes and complementary as one commodity, but it makes the utility analysis unrealistic. For example, tea and coffee are substitute products. When there is a change in the stock of any one product, there is change in the marginal utility of both the products. Suppose there is increase in the stock of tea. There will not only be fall in the marginal utility of tea but also of coffee. Similarly, a change in the stock of coffee will bring a change in the marginal utility of both coffee and tea. The effect of one commodity on the other, and vice versa is called the cross effect. The utility analysis neglects the cross effects of substitutes, complementaries and unrelated goods. This makes the utility analysis unrealistic. To overcome it, Hicks constructed the two-commodity model in the indifference curve approach.

(3) Money is not measuring indices of Utility:

According to Marshall Utility is measured in terms of money, but money is an incorrect and imperfect measure of utility because the value of money often changes. If there is a fall in the value of money, the consumer will not get the same utility from the homogeneous units of a commodity at different times. Fall in the value of money leads to rise in prices. Besides, if two consumers spend the same amount of money at a time, they will not be getting equal utilities because the amount of utility depends upon the intensity of desire of each consumer for the commodity. For instance, consumer A may be getting more utility than B by spending the same amount of money if his intensity of desire for the commodity is greater. Therefore, money is an imperfect and unreliable measuring rod of utility.

(4) Marginal Utility of Money is not constant:

The utility analysis assumes that the marginal utility of money remains to be constant. Marshall supported this argued that a consumer spends only a small portion of his income on a commodity at a time so that there is an insignificant reduction in the stock of the remaining amount of money. But the fact is that a consumer does not buy only one commodity but a number of commodities at a time. In this way when a major part of his income is spent on buying commodities, the marginal utility of the remaining stock of money increases. For instance, every consumer spends a major portion of his income in the first week of the month to meet his domestic requirements. After this, he spends the remaining amount of money wisely. It implies that the utility of the remaining sum of money has increased. The assumption that the marginal utility of money remains constant is away from reality and makes this analysis hypothetical. Thus, Marshall's demand theorem and constant marginal utility of money are incompatible except in a one commodity case.

(5) Man is not rational:

The utility analysis is based on the assumption that the consumer is rational who wisely buys the commodity. He has the capacity to calculate the dis-utilities and utilities of different commodities, and buys only those units which give him greater utility. This assumption is also unrealistic because no consumer compares the utility and disutility from each unit of a commodity while buying it. In fact, he buys them under the influence of his desires, tastes or habits. Moreover, consumer's income and prices of commodities also influence his purchases. Thus, the consumer does not buy commodities rationally. This makes the utility analysis unrealistic and impracticable.

(6) Consumer not of Calculating Mind:

This analysis assumes that the consumer can calculate the utilities of different units of a commodity and purchases those which provide him more utility. However, no consumer calculates in this manner while buying commodities. But he purchases them according to his income and their prices.

(7) Utility Analysis neglects the Income Effect, Substitution Effect and Price Effect:

The greatest defect in the utility analysis is that it ignores the study of income effect, substitution effect and price effect. The utility analysis fails to explain the effect of a rise or fall in the income of the consumer on the demand for the commodities. It thus neglects the income effect. Furthermore, in case of the change in the price of one commodity, there is a relative change in the price of the other commodity, the consumer substitute's one for the other. This is the substitution effect which the utility analysis fails to discuss because it is based on one-commodity model. Besides, when the price of one commodity changes, there is change in its demand and in the demand for related goods. This is the price effect which is also ignored by the utility analysis. Hence, it fails to analyse the income and substitution effects of a price fall via the increase in the real income of the consumer.

(8) Utility Analysis fails to clarify the Study of Inferior and Giffen Goods:

Marshall's utility analysis of demand does not clarify the fact as to why a fall in the price of inferior and Giffen goods leads to a decline in its demand. Marshall failed to explain this paradox because the utility analysis does not discuss the income and substitution effects of the price effect. This makes the Marshall's utility analysis incomplete.

(9) The Assumption that the Consumer buys more Units of a Commodity when its Price falls is Unrealistic:

The utility analysis of demand is based on the assumption that the consumer buys more units of a commodity when its price falls. It may be true in the case of food products like oranges, bananas, apples, etc. but not in the case of durable goods. If the price of bicycle, radio, etc. falls a consumer will not buy two or three bicycles or radios. It is another thing that a rich man may buy two or three cars, pairs of shoes and variety of cloths, etc. but he does so irrespective of the fall in their prices because he is rich. The argument therefore does not hold good on ordinary persons.

(10) This Analysis fails to explain the Demand for Indivisible Goods.

The utility analysis breaks down in the case of durable consumer goods like scooters, transistors, radio, etc. because they are indivisible. The consumer buys only one unit of such commodities at a time so that it is neither possible to calculate the marginal utility of one unit nor can the demand schedule and the demand curve for that good be drawn. Hence, the utility analysis is not applicable to indivisible goods. These defects in the utility analysis led economists like Hicks to explain the demand analysis of the consumer with the help of indifference curve approach.