Pigovian Welfare Economics

Welfare economics is closely related to ethics but Pigou does not clarify it. Welfare economics is essentially a normative study in which value judgements and inter personal comparisons are made. By not relating these concepts with his notion of welfare, Pigou's economics of welfare is not considered as an objective study of the causes of welfare.

Marshall made the concept of consumers surplus as the central tool of his welfare analysis. Marshall considered the community's welfare to be maximum when its satisfaction is maximum.

There were two basic assumptions of this maximum welfare analysis of Dr. Marshall:

1. Equal sums of money measure equal utilities to all and

2. A fall in the price of the product results in a fall in output and hence loss of satisfaction.

Marshall advocated that an industry which is working under increasing returns must produce beyond its equilibrium point and an industry working with diminishing returns should stop producing before their equilibrium output. For this he suggested the policy of giving a bounty to increasing returns industry and levying a tax on the industries subject to diminishing returns. The proceeds of the tax could be used for giving bounties.