

Comparison between Marshallian Utility Analysis and Indifference Curve Analysis

Indifference Curve Analysis

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- Though the two approaches are different in many respects, there are some similarities in these two theories of demand. First, both these theories assume that consumers are rational and therefore try to maximize utility. Second, both these theories use psychological or introspective method to explain consumer's behavior. Thirdly, both these theories of demand assume in some form diminishing marginal utility or desire for a commodity as a consumer takes more units of a commodity. In this connection it is generally believed that the principle of diminishing marginal rate of substitution is similar to the law of diminishing marginal utility of Marshallian utility analysis.

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❖ Superiority of Indifference Curve Analysis

1. Ordinal vs Cardinal Measurability of Utility.

- Marshall assumes utility to be cardinally measurable.
- According to the critics, utility is a psychological feeling and the precision in measurement of utility assumed by Marshall and other is therefore unrealistic.
- utility is merely orderable and not quantitative

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2. Analysis of Demand without Assuming Constant Marginal Utility of Money

- Marshallian demand theorem cannot genuinely be derived from the marginal utility hypothesis except in one commodity model, without contradicting the assumption of constant marginal utility of money.
- On the other hand, indifference curve technique using ordinal utility hypothesis can validity derives the demand theorem without the assumption of constant marginal utility of money. The abandonment of assumption of constant marginal utility of money enables the indifference curve analysis to enquire a more general demand theorem.

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3. The indifference technique splits up the price effect analytically into its two component parts - substitution effect and income effect.

But, Marshall by assuming constant margin utility of money ignored the income effect of a price change.

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4. Enunciation of a more general and adequate demand theorem.

- Marshall could not account for “Giffen Paradox”.
- The indifference curve technique by distinguishing between the income and substitution effects of the price change can explain the Giffen case.

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5. Implications of a Price Change in terms of Income and Welfare Increment.

6. Hypothesis of Independent Utilities Given Up.

7. Analysis of Consumer's Demand with Less Restrictive and Fewer Assumptions.

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- **Critique of Indifference Curve Approach**

- The above discussion shows that the indifference curve approach is more realistic, more scientific and simpler; the approach suffers from certain shortcomings and drawbacks.

- i. It is pointed out that there is nothing new in indifference curve approach. Instead of the term utility, indifference curve has introduced the term preferences. The old law of diminishing marginal utility is substituted by diminishing marginal rate of substitution. Robertson says that it is merely old wine put in new bottle.

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- ii. It is unrealistic to assume as Indifference curve approach assumes that consumer is familiar with entire his entire preference schedule.
- iii. Indifference curve approach can demonstrate and analyse effectively only in simple cases involving two goods. In case of three goods, three dimensional diagram is required which is tedious. However, when more than three goods are involved, geometry altogether fails.

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- iv. Like old theory, indifference curve analysis is also built on the assumption that consumer behaves in rational manner when it comes to spend his money income on goods.
- v. The indifference curve analysis is not very amenable to empirical research.

THE END