Arthur C. Pigou (1877-1959)

Arthur Pigou was born 18 November 1877 on the Isle of Wight, and died 7 March 1959 in Cambridge, England. After being educated at Harrow, he went on to study at King's College, the University of Cambridge, where by 1900, he had obtained a first in both the Historical and Moral Sciences Tripos. He was elected as a Fellow of King's College in 1902, where he spent the rest of his academic life. He published over 12 books and contributed to over 100 articles during his career, holding an appointment as Professor of Political Economy for 35 years, having succeeded Alfred Marshall to the chair in 1908. Among his contemporaries, the best-known was John Maynard Keynes, whose lectureship at Cambridge Pigou privately funded until the former was elected Fellow of King's College in 1909.

Pigou is most commonly remembered for placing welfare at the center of the discipline of economics. Based on the premise that utility was measurable, he proposed in *Wealth and Welfare* (1912) that improved economic welfare would result from: an increase in national income, an increase in the absolute share of national income going to the poor; and, a reduction in the variability of national income, especially the share received by the poor. Pigou expanded on these ideas in *The Economics of Welfare* first published in 1920, where he argued that economic welfare will not be maximized if there is a divergence between what he termed the marginal net social product and marginal private net product of economic activities. Importantly, he highlighted the notion of *externalities* with reference to the possibility that, "…costs are thrown upon people not directly concerned, through, say, uncompensated damage done to surrounding woods by sparks from railway engines…" (Pigou, 1932, p. 134), and also provided the argument for what is now termed a *Pigouvian tax* (*subsidy*), "…when competition rules and social and private net product at the margin diverge, it is theoretically possible to put matters right by the imposition of a tax or the grant of a subsidy…,” (Pigou, 1932, p.381).

Pigou’s analysis of welfare was subsequently displaced by the writings of economists such as Lionel Robbins who challenged his approach as being unscientific on two counts: it was based on utility being measurable, and it analyzed what “ought to be” as opposed to “what is”, i.e., Pigou’s propositions were normative, and hence value-laden. Also, after his death, Pigou’s policy prescription for externalities was criticized by Ronald Coase (1960) who argued that assignment of property rights would allow negotiation between parties, resulting in *internalization* of an externality.

Although overshadowed by Keynes’ *General Theory* (1936), Pigou also made a significant contribution to macroeconomics. Defining real balances as the sum of the money supply and government bonds relative to prices, he developed the so-called *Pigou effect*, whereby an economy could escape the *liquidity trap*. Specifically, if an aggregate demand shock causes unemployment to rise, prices will fall, thereby increasing real balances, raising consumption, and pushing the economy back towards full employment (Pigou, 1943).

References:

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Pigou, A.C. 1932. *The Economics of Welfare*, London: Macmillan (fourth edition).
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