



ECONLOG PERMANENT LINK | SEPTEMBER 13, 2010

Printable format for http://econlog.econlib.org/archives/2010/09/austerity_for_1.html

Austerity for Liberty

Bryan Caplan

FAQ: Print Hints

Suppose that in 2005, Bush managed to "privatize Social Security" to a politically astonishing degree. Under the hypothetical legislation:

1. Workers are free to divert 100% of their future payroll tax into private accounts.
2. Workers are free to immediately ask for the present value of their future SS checks, as long as they put their money in reputable investments.

Let's say that half the people in the SS system took full advantage of the new rules.

Question: After the 2008 crash and subsequent fall-out, how would the political system have responded? I'll bet it would have made TARP look small. Tens of millions of people would have lost half their assets and half their retirement income as a "direct result" of Bush's legislation. The government wouldn't have stood idly by. In all likelihood, it would have enacted a **kilo-page** relief measure to tortuously compensate (some of) the losers, randomly increase regulation on financial markets, and bribe a hundred fence-sitting legislators.

This scenario and others like it make me suspect that "constructive" free-market reforms like Social Security privatization, school choice, Medicare vouchers, etc. are largely a waste of libertarians' political capital. They pose two great risks:

1. If anything goes wrong, the market will receive all the blame. The political backlash could easily lead to policies more statist than ever.
2. In practice, the government will never implement a transparent free-market reform. Even an idea as simple as "give people the freedom to invest their own payroll taxes in a private account" will quickly morph into a kilo-page Congressional boondoggle. This further increases the chance that something *will* go wrong. And when it does, the market will take all the heat.

Depressing? I have a better way. Instead of pushing for "constructive" free market reforms, libertarians should doggedly focus on *austerity*: opposing spending increases, and pushing spending cuts. Instead of trying to "privatize" Social Security, for example, libertarians should push for lower benefits, a higher retirement age, and **means testing**. Instead of pushing for school choice, libertarians should try to restrain/shrink education budgets and push user fees. If libertarians have any political success, this will *automatically* expand the role of the market. After all, the less government does for people, the more they will do for themselves. Dissatisfied with government provision, people will save more for their own retirement and spend more on private education. In the limit, once the flow of government money ceases, voluntary exchange is all that's left.

Austerity has two major advantages over more "constructive" free-market reforms:

1. If anything goes wrong, public opinion is less likely to blame the market. Government decided to spend less on X; how is that the market's fault? Logically, people could simply reframe their complaints. But psychologically, it's easier to point fingers at markets directly sanctioned by government action than markets indirectly prompted by government *inaction*.
2. Congress is also less likely to use austerity as an excuse for new kilo-page legislation. Officially expanding market options takes "sweeteners." Mere budget cutting, not so much.

To be fair: I understand why libertarians promote "constructive" free-market reforms. They sound better and feel nicer. Rhetorically speaking, a person can promote SS privatization and still be "pro-retiree," or promote school choice and still be "pro-education." The person who pushes for cuts in retirement and school budgets effectively forfeits these rhetorical options. But if you actually want to promote liberty, austerity seems like the option most likely to deliver it.

HT: Partly inspired by a lunch with [Steven Teles](#).

TRACKBACKS (0 to date)

TrackBack URL: <http://econlog.econlib.org/mt/mt-tb.cgi/3990>

COMMENTS (20 to date)

Latest Comment

Hyena writes:

Doesn't this fundamentally misunderstand the history of government growth?

Posted September 12, 2010 11:24 PM

Scott Wentland writes:

Great post!

But to play devil's advocate I have a few questions:

1) Won't public opinion have a problem with the austerity politicians because they aren't "doing something"? Both the progressives and libertarians are politicians that "have a plan" and "get stuff done," giving them a distinct rhetorical advantage in campaigns.

2) How are school choice and medicare vouchers subject to market cycles (and its potential backlash) if they are still *funded* by government? Granted government revenues fall during recessions, and there is some resentment about markets in general, but I think the "market failure" link is not as quite as clear here as the privatization of SS example.

3) What about the Krugman-type claims that it was the austerity folks that prevented the stimulus (or any program for that matter) from being bigger and more effective? Rhetorically, isn't austerity setting yourself up to be the fall guy when government action fails?

Posted September 13, 2010 12:40 AM

Peter writes:

Australia has privatised social security. All employees have a minimum 9% of their salary, up to a maximum amount, deducted by their employer and paid into a superannuation fund. You can choose your super fund or even set up your own.

Naturally, lots of people recently had big falls in their super, and reportedly many near retirees will have to stay at work longer. However, the government has not stepped in to make up the shortfalls. So perhaps you are worrying about nothing.

Posted September 13, 2010 1:16 AM

david writes:

Apropos:

[Goh] explained that the government allowed the use of CPF money for investment because interest rates at the time were "on the low side, and there was pressure for CPF to open up".

Unfortunately, most people lost money because they are not savvy investors, he said.

Posted September 13, 2010 1:50 AM

Troy Camplin writes:

Cut spending, and people will blame the cut in spending, and boom, we get a kilo-page etc.

Don't underestimate statist shenanigans to expand their power. It's always one excuse or another.

Posted September 13, 2010 2:28 AM

geckonomist writes:

question: What are "reputable investments"?

Would I be allowed to invest in a fine property on the beach in Bali ?

If not, what's libertarian about that private account scenario?

Posted September 13, 2010 4:13 AM

RPLong writes:

I agree with Bryan Caplan here. Starving the government to death is the best way out, as far as I'm concerned.

Posted September 13, 2010 7:12 AM

Tyler In Chicago writes:

Congratulations Bryan, you've invented ordo-libertarianism. I hope it lasts longer than liberalitarianism did.

Posted September 13, 2010 9:10 AM

Hugh Watkins writes:

How about putting in some intermediate steps:

- 1) rejig SS so that what you pay in is what you get out (plus interest of course).
- 2) send people annual statements to show where they are and what they can hope to receive when they reach retirement age.
- 3) deal with hard cases out of general taxation and not through murky redistribution through SS.

Once this system is in place people will know what they have to do privately to get to where they want to be at retirement.

Posted September 13, 2010 9:49 AM

Brian Clendinen writes:

I really don't see the logic of these counterfactuals. One, the Dutch the Swedes have school vouchers, does your argument hold true for them? If not why is the U.S. different?

The Swiss have an insurance voucher program and Argentina has a private SS option in addition to Australia a discussed. How due the same questions above apply to these cases?

I agree with your argument that small reforms have a lot better chance of having a real impact. Considering how our political systems works your suggestions have a better chance of passing. However, that still should not stop us from pushing for more radical reforms.

I think school vouchers are much more politically viable. The only reason here in Florida we don't have them is because the State Supreme court found them unconstitutional. The program was only for students of failing schools and this was quite a few years ago. I think most likely we would of seen this program expanded by now if not for the court decision. So it is not the public or politicians but the courts who are blocking reforms. I could see the same thing happening with Medicare/Medicaid vouchers, the courts overruling congress.

Posted September 13, 2010 10:07 AM

B.B. writes:

I think the real problem with Social Security is not that it is run by the government but that it is a simple tax-and-transfer scheme.

Let's side aside uncertain lifetimes for simplicity.

Everybody puts in a fixed percentage of paycheck into an account. The government pays a fixed 1% real rate of return (about the historical average for real Tbill rates). People retire whenever they want. The account turns into a fair-value annuity at retirement.

You don't have to worry about market crashes or bailouts. But you don't have to worry about tax hikes either: the system is always 100% funded. People get out what they put in, with a return that the government can get.

The government need only raise taxes to pay the interest. Or the government could invest the funds.

It is not exactly free market, but it not a pure tax and transfer scheme either.

Posted September 13, 2010 10:31 AM

Rob writes:

Fantastic post. It is a bit depressing, though. I don't see pushing austerity as any more politically feasible than constructive market solutions, because of entrenched interest groups (e.g. farm subsidies) and the politician's fallacy: "Something must be done; this is something; therefore it must be done."

"If anything goes wrong, public opinion is less likely to blame the market." That may be true. But unfortunately, it seems that when problems arise, whether due to market failure or not, voters like to see governments spend big money trying to fix them. Even if that government spending might exacerbate those same problems.

Politicians have to be seen to be doing something. To a lot of voters, inactivity/austerity appears to be a sign of impotence. It's a bias that, to me, accounts for a lot of government sprawl ("growth" sounds too positive).

Posted September 13, 2010 10:50 AM

Philo writes:

"If anything goes wrong, public opinion is less likely to blame the market." If a good measure is adopted and then something goes wrong, the public will blame the good measure, whether it was "austerity" or "free-market reform," and it will be undone (or worse).

"I understand why libertarians promote 'constructive' free-market reforms." They want people to appreciate markets and lose some of their enthusiasm for socialism; they hope the process of "promotion" will have educational value. Success in their ideological effort would undercut your worries about the likely socialistic aftermath of free-market reforms when something went wrong. Unfortunately you are right that such success is very unlikely.

But your view points to *quietism*, not an alternative form of activism.

Posted September 13, 2010 10:52 AM

English Professor writes:

I think Bryan is absolutely right about what would have happened if the privatization of SocSec had been carried through. On 10 Oct 2008, during the panic that followed the failure of Lehman Brothers, Arnold wrote a post on "Stock Markets and Social Security." Here was my comment at that time:

"What you say would be fine if private retirement accounts were not a political issue. I completely agree that on the whole people would be better off with private retirement accounts, but if we're talking economics here, it has to be 'public choice' economics. Don't forget, they would have to be created by political action, and those who voted for them would be held responsible for any short-term declines. Now, the incredible volatility of the market makes it clear that the traders themselves are pretty close to panic; you would have to expect the citizenry to be much more irrational than the traders, so their fear would be double or triple what we're seeing now. They would be demanding a bailout of their retirement funds. And what politician today would have the nerve to tell them to wait until the market turned?"

I believe that the privatization scheme would have crumbled during the dive that took the S&P 500 down to the 600s.

Posted September 13, 2010 11:59 AM

NFB writes:

Very good point in this article. Government-backed privatization is almost a contradiction in terms - as Professor Caplan puts it, the result is "kilo-page" legislation which flouts the intended elegance of a market-based solution.

I agree that austerity is probably a more productive avenue than constructive reform, but it has been a tough pill to swallow when applied elsewhere. There have been widespread protests of government austerity measures in Europe; examples are easy to come by. America is a different setting, of course. Perhaps as reality sets in, that the financial crisis won't disappear unless we're willing to make some policy sacrifices, austerity measures will become more politically feasible.

Posted September 13, 2010 12:12 PM

Jeff writes:

Doesn't this fundamentally misunderstand the history of government growth?

Yeah, this post sounds like Bryan wants to trade one strategy he doesn't think will work for another strategy he ought to know doesn't work.

Not exactly what I'd call an improvement.

Posted September 13, 2010 12:22 PM

Dan Weber writes:

2. Workers are free to immediately ask for the present value of their future SS checks, as long as they put their money in reputable investments.

I'm not sure enough money exists in the world to manage this. The money to pay those promises has not been collected yet.

Posted September 13, 2010 12:24 PM

flocina writes:

I agree.

IMO the biggest problem with Gov. schools is that they spend too much.

IMO the biggest problem with SS is the tax that funds it is too big a burden.

Solutions:

Welfarize SS - everyone gets the same minimum payout. Also raise the eligibility age.

Charge for Gov schools. You cannot subsidize everyone so why not charge the rich and middle class for Gov. schooling.

Posted September 13, 2010 12:27 PM

Ryan writes:

Unfortunately, this is not **a novel idea**. This is all I could think about as I read Bryan's post. Maybe I'm mistake in that he doesn't believe it's novel but, just a good tack?

Posted September 13, 2010 2:49 PM

Sheldon Richman writes:

Bryan, you say that under austerity, "If anything goes wrong, public opinion is less likely to blame the market. Government decided to spend less on X; how is that the market's fault?"

Won't people blame market advocates for starving the beast? I fear we won't get off so easily.

Posted September 13, 2010 3:13 PM

[Return to top](#)

Copyright © 2003-2010

Liberty Fund, Inc.

All Rights Reserved. Not for redistribution. For reprint information, contact the webmaster@econlib.org