

# False economic security and the road to serfdom

*But the policies which are now followed everywhere, which hand out the privilege of [economic] security, now to this group and now to that, are nevertheless rapidly creating conditions in which the striving for security tends to become stronger than the love of freedom. The reason for this is that with every grant of complete security to one group the insecurity of the rest necessarily increases.*

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Friedrich Hayek (1944). *The Road to Serfdom*.

In Bruce Caldwell (ed.), *The Road to Serfdom*, II

(Liberty Fund Library, 2007): 153.

Indispensable to the creation, maintenance, and growth of widespread prosperity is an economic system that uses scarce resources as efficiently as possible to create goods and services that satisfy as many consumer demands as possible. To the extent that the economic system encourages, or even permits, productive resources to be wasted, that system fails to achieve maximum possible prosperity. If, say, large deposits of petroleum beneath the earth's surface remain undetected because the economic system doesn't adequately reward the human effort required to find and extract such deposits, then people will go without the fuel, lubricants, plastics, medicines, and other useful products that could have been—but are not—produced from this petroleum.

The system that best ensures that resources are used as efficiently as possible is free-market capitalism—an economic system based on transferrable private property rights, freedom of contract, the rule of law, and consumer

sovereignty. This last feature of free-market capitalism is the right of each consumer to spend her money as she sees fit. She can spend as little or as much of her income as she chooses (in order to save whatever she doesn't spend), and she can change her spending patterns whenever and in whatever ways she likes.

In short, consumer sovereignty means that the economy is geared toward satisfying consumers, not producers. This aspect of a market economy is important to emphasize because we are often told otherwise, namely, that a market economy is geared to benefit mainly producers. Yet in well-functioning economies producers—including entrepreneurs, investors, businesses, and workers—are not ends in themselves. Their activities, as valuable as these are, are means rather than ends. These activities are justified and valuable only if, only because, and only insofar as these produce outputs that consumers choose to buy. If consumers change their spending patterns (as they frequently do), producers must change to accommodate the new ways that consumers spend.

The freedom of producers to respond to, and even to anticipate, consumer demands is so vitally important for the success of the market economy that people often regard the case for economic freedom to be chiefly a case for the freedom of *business*. This is a mistake. At root, the case for economic freedom is a case for the freedom of *consumers*.

Of course, because maximum possible consumer freedom entails the freedom of entrepreneurs and businesses to compete vigorously for consumers' patronage, the defense of free markets often requires the defense of profits as well as of business's freedom to experiment with different ways of earning profits. Oil companies not allowed to earn sufficient profits from finding new oil deposits won't invest the resources required to find those deposits. Upstart entrepreneurs prevented by licensing restrictions from entering a profession will be unable to offer their services to consumers who might find those services appealing. The defense of profits and business freedom, though, is a defense primarily of the chief *means* that the market uses to ensure that consumers are served as well as possible.

The fact that each person's livelihood is tied disproportionately to what he or she produces rather than to what he or she consumes creates a practical problem, however. Each person, as a producer, works only at one or two occupations; each person earns an income only from one or two sources. Yet each person, as a consumer, buys thousands of different items.

*I always worry about what  
the customer wants!*



*Why don't I have more customers?  
I love my products —  
and so should they!*

A change in the price of any one or a few consumer goods has much less impact on the well-being of an individual than does a change in the price of what that individual is paid for what he produces or for the labour services he sells. As a consumer I'd obviously prefer that the price of my favourite hamburgers or music downloads not rise by 20 percent, but such price hikes won't harm me very much. In contrast, as a producer I'd suffer substantially if my income fell by 20 percent. I'm much more likely to complain bitterly about—and to resist—a fall in my income than I am to complain about and resist a rise in the prices of the things I buy as a consumer.

Politicians in democratic countries naturally respond to these concerns. People's intense focus on their interests as producers, and their relative inattention to their interests as consumers, leads them to press for government policies that promote and protect their interests as producers.

If government policies that protect people's interests as producers are limited to keeping them and their factories, tools, inventories, and other properties safe from violence, theft, fraud, and breach of contract, then there is no danger. Indeed, such protection of producers—along with assurances against their being taxed and regulated excessively—is essential for economic prosperity. Trouble arises, however, when government seeks to protect producers (including workers) from market forces—when government aims to shield

producers from having to compete for consumer patronage. Such protection promotes not free-market capitalism, but crony capitalism.

For government to ensure that some producers—say, wheat farmers—suffer no declines in their economic well-being requires that it restrict the freedoms of consumers, of other producers, or of taxpayers. Special privileges granted to wheat farmers must come in the form of special burdens imposed on others.

Consumers who exercise their freedom to buy fewer loaves of wheat bread (say, because they have grown to prefer rye bread) will cause the incomes of wheat farmers to fall, and may even cause some wheat farmers to go bankrupt. To protect wheat farmers from this consequence of consumer sovereignty obliges government to take steps to artificially prop up the demand for wheat. To artificially prop up the demand for wheat requires, in turn, policies such as punitive taxes on rye farmers (to discourage them from producing so much rye), restrictions on the importation from foreign countries of rye, or even requirements that consumers continue to buy at least as much wheat bread today as they bought yesterday.

Whatever particular policies government uses to protect wheat farmers from the consequences of consumers' voluntary choices, this protection *must* come at the expense of others. Other people—either as consumers, as producers, or as taxpayers—are also made a bit less free by government's effort to protect wheat farmers from the downside of economic change.

If government protects only wheat farmers from competition—if government exempts only wheat farmers from having to follow the same rules of a market economy that are obeyed by everyone else—the resulting damage to the economy (especially in large advanced countries such as Canada and the United States) will be minimal. Wheat farmers will indeed each be noticeably better off as a result, while almost everyone else—as individual consumers or taxpayers—will suffer so little as a consequence that the pain might well go unnoticed.

Politicians will receive applause and votes and much other political support from wheat farmers without suffering a corresponding loss of popularity, votes, and political support from non-wheat-farmers. Politicians will then find it easy and attractive to gain even more political support by granting similar protection to some other producer groups—say, to steel workers or to airline pilots.

As government exempts more and more producers from the rules of the market—that is, as government relieves more and more producers from the necessity of having to compete, without special privileges, for consumers' patronage, and to enjoy the benefits of their successes and suffer the consequences of their failures—the total costs of such protection rise and, hence, become increasingly noticeable. The slowdown in economic growth for ordinary men and women becomes conspicuous. People grow more concerned about their economic futures.

Seeing government spread its protective net over an ever-increasing number of producers, those producers who haven't yet received such protection naturally begin to clamour for it. First, these producers understandably feel as though government is unfairly mistreating them by not granting to them what it grants to so many other producers.

Second, the greater the number of producers who are protected from the downside of economic competition, the greater the negative impact of that protection on consumers and the relatively few producers who are not yet protected. If the full burden of adjusting to economic change is focused on an increasingly smaller number of people, the extent to which each of those people must adjust is greater than if the burden of adjusting to economic change is spread more widely.

If government remains committed to protecting from the downside of economic change all who clamour for such protection, the powers of government must necessarily expand until little freedom of action is left to individuals. It is this stubborn commitment to protect larger and larger numbers of people from the negative consequences of economic change that Hayek argued paves the road to serfdom.

That government must have extraordinary discretionary power over vast areas of human action if it is to try to protect large numbers of people from the downside of economic change is clear. Any time entrepreneurs invent new products that threaten the market share of existing products the owners of the firms that produce those existing products will suffer lower demands for their services. So, too, will workers in the factories that manufacture those existing products. The incomes of these owners and workers will fall, and some might lose their jobs, as a result of the introduction of new, competitive products.

The very same process is true for *any* economic change. New imports from abroad threaten domestic producers of products that compete with these imports. Labour-saving technologies threaten the livelihoods of some workers whose human skills compete with the tasks that can now be performed at low-cost by these new techniques. Changes in population demographics—say, an aging population—cause the demands for some goods and services (for example, baby strollers and pediatric nurses) to fall as they cause the demands for other goods and services (for example, large sedans and cardiac surgeons) to rise.

Even simple everyday shifts in consumer tastes away from some products and toward other products unleash economic changes that inevitably threaten some people's incomes and economic rank. The growing popularity several years ago of the low-carbohydrate Atkins diet shifted consumer demand away from foods such as bread and beer and toward low-carb foods such as chicken and beef. As a consequence, bakers and brewers suffered income losses; ranchers and butchers enjoyed income gains. If government were intent on protecting bakers and brewers from experiencing these income losses, it would have either had to somehow stop people from changing their eating habits, or raise taxes on the general population to give the proceeds to bakers and brewers.

Regardless of the particular methods it employs, a government that is resolutely committed to protecting people from any downsides of economic change requires nearly unlimited powers to regulate and tax. As long as people have the desire and can find some wiggle room to change their lives for the better—for example, to change their diets, to invent technologies to conserve the amount of labor required to perform certain tasks, or to increase the amounts they save for retirement—some fellow citizens are likely suffer falling incomes as a result. The only way to prevent any such declines in income is near-total government control over the economy.

Unfortunately, because economic growth is economic change that requires the temporarily painful shifting of resources and workers from older industries that are no longer profitable to newer industries, the prevention of all declines in incomes cannot help but also prevent economic growth. The economy becomes ossified, static, and moribund. So achieving complete protection of all citizens at all times from the risk of falling incomes means not only being ruled by an immensely powerful government with virtually no

checks on its discretion, but also the eradication of all prospects of economic growth. Inevitably, at the end of this road paved with the good intention of protecting all producers from loss lies not only serfdom but also widespread poverty.