

*On some
unintended
consequences
of the welfare state*

*by
Kurt R Leube*

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Foreword

The *Occasional Paper* series is designed to bring to South African audiences writings of import which might not otherwise circulate widely in this country. Kurt Leube's *Paper* is a highly pertinent example.

Only recently Deputy President Jacob Zuma called for a 'moral regeneration' in South Africa. He feared that our sense of *ubuntu*, where traditionally we have had a society strongly community-oriented towards family and extended family responsibility, was being eroded. Zuma was right to be worried. The nation's government is currently considering extending the level of welfare provision.

Leube points out (p.9) that much of Europe and America has already gone down a similar path. In France the legal term *solidaire*, which characterised the fellow-feeling and obligation of shared responsibility for the total debt of families or small organisations in the mid-19th century, has been replaced by Comte's 'social solidarity'. The latter implies not obligation to others in the 'little platoons' of which we are members, but rather the expectation as of right that the anonymous taxpayer, through the welfare state, will provide the resources for any form of selfish and irresponsible life-style choice we care to adopt.

Economic liberals (for example Britain's Arthur Seldon) have in the past regarded the welfare state as a transient phenomenon. Individuals provided with a safety net against poverty will, as they grow richer, opt for private provision in health, education and welfare in order better to satisfy their individual preferences. They will reassume individual responsibility to attain the benefit of choice in accord with their individual value systems.

Leube's prognosis (pp.7-8), the 'moral hazard of being honest', is much gloomier. The various forms of welfare raise problems of collective action. Politicians can gain votes and power by competing with each other to offer ever more 'free' services. Individual voters may prefer a different set of offerings, but will not refuse those provided by government since to do so would be irrational given that the 'price' to them at the point of consumption is zero. On the other hand, to oppose the principle in argument would be a high-cost strategy with little prospect of success.

There is worse. It is not only people's behaviour which is changed by the politically attractive presence of so-called social welfare in health, education, pensions and other services or monies provided. *Ubuntu* and *solidaire*, people's value systems, preferences and standards of morality, are also altered (see pp.14-16). Adam Smith emphasised that individuals are selfish but that selfishness results in market exchanges which benefit all (*The Wealth of Nations*). Meanwhile that selfishness is governed and monitored so that behaviour patterns meet with the approval of the 'impartial spectator' (*The Theory of Moral Sentiments*). The impartial spectator is, of course, one's conscience, embodied in *ubuntu* and in the notion of *solidaire*. The human conscience, Smith explained, has evolved over time to meet the joint and several best interests of individuals and society.

David Hume stressed the importance of the evolution of values: 'the rules of morality are not the conclusions of our reason'. Hayek agreed and warned that 'we can never synthetically construct a new body of moral rules'. But there are attempts to do so by those who believe they have wisdom superior to that of their fellows. One symptom of this, said Hayek, is the substitution of the word 'social' for the word 'good'. To have a good conscience, or merely a conscience, implies the impartial spectator approves of our actions. To have a social conscience implies that some second party will approve of our actions as they affect other people or some third party. The second party is usually some form of greater collective, with powers, while the impartial spectator is a traditionally-developed, internalised yardstick.

The welfare state, with the behaviour patterns it engenders and supports, does not brook opposition. It exercises insidious monopolistic powers, not at the point of a gun, but by appealing to our intrinsic selfishness while simultaneously altering our value systems. As individuals we lose our freedom to experiment and make our own life-style choices, bearing the costs and obligations of our humanity, while sharing the benefits and privileges.

Leube's argument (pp.14-16) in the current climate is a brave one. The welfare state also facilitates individual life-style choices. But the choices it facilitates and encourages are unconstrained and 'costless' to the individual while detrimental to all. It effectively removes the freedom to make constrained choices from the decision set. And it encourages hedonistic life-style choices which are apparently attractive but which damage all our freedoms. Whether this damage is caused by the Moloch of ever increasing taxation and government spending, or the detriment is caused by the destruction of *ubuntu* and *solidaire*, the welfare state, Leube concludes, has unintended consequences and should be opposed.

Leube's arguments will not appeal to either unthinking libertarians or democratic socialists. They are not necessarily acceded to by the Directors, members or staff of the Free Market Foundation. Nevertheless the *Paper* will make a valuable contribution to the current South African debate which Deputy President Zuma is attempting to lead.

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Kurt R Leube, a native of Austria, is internationally recognised as a leading authority in the tradition of the Austrian School of Economics and as one of the closest collaborators and disciples of Friedrich A von Hayek. Educated in Germany and Austria, he works presently as Research Fellow at ICER, Torino (Italy), Prof of Economics (*emeritus*) California State University, Hayward (USA), and as Academic Director of the FA von Hayek Institute (Austria). He specialises in Austrian Economics and the History of Economic and Legal Thought.

1 Introduction

If government wants not merely to facilitate the attainment of certain standards by the individuals but to make certain that everybody attains them it can do so only by depriving individuals of any choice in the matter.

FA von Hayek

Nowadays few regard the old socialist ideas of central economic planning and nationalization as a way to promote more efficient production, greater equality, or even a more ‘just’ distribution of income. But a number of worn conceptions are still prevalent, notably including the deeply-rooted constructivist belief that every social problem can be solved by ‘social engineering’ or just by throwing government money at it. This seems to have penetrated the minds of social scientists, intellectuals and politicians. Although not openly advocating economic planning, many of them hold that ‘social legislation’ or ‘social politics’ can be used in a more subtle way to achieve an already predetermined end: the perfected welfare state.

In a short essay already drafted in early 1935 but published much later, FA von Hayek showed that the idea of central planning, aimed at achieving particular social targets, will necessarily result in ever-increasing coercion of men by the state and the loss of individual and political freedom. In the printed version of his “Freedom and the Economic System” (1938), Hayek warned us that “the wide popularity which the idea of central direction of all economic activity enjoys today is easily explained by the two facts that, on the one hand, people are promised by experts a greater amount of welfare if industry is ‘organized’ along rational lines, and, on the other, that it is so obvious that those particular ends which each individual most desires can be achieved by planning. But if people agree about the desirability of planning in general, their agreements about the ends which planning is to serve will in the first instance necessarily be confined to some general formula like ‘social welfare’, the ‘general interest’, the ‘common good’, greater equality or justice etc. Agreement on such a general formula is, however, not sufficient to determine a concrete plan, even if we take all the technical means as given”.¹

Yet nowadays popular and irrepressible superstitions about a “Third Way”² between all kinds of modern Socialisms and something that they tend to call ‘free markets’ dominate the public debate in transition countries. The concept of an advanced European welfare state seems to be perceived as the most appealing model at hand. I shall concern myself here chiefly with some of its conceptual contradictions, and I shall attempt to draft a few suggestions for a breakaway.

¹ See FA von Hayek “Freedom and the Economic System”, *The Contemporary Review*, Vol.153, London 1938.

² See Vaclav Klaus “The Third Way and Its Fatal Conceits”, in: *Vordenker einer neuen Wirtschaftspolitik. Festschrift für Christian Watrin*, Kurt R Leube, Ed., The International Library of Austrian Economics, Vol.5, FAZ-Buch, Frankfurt/M. 2000.

2 *A brief and sketchy historical outline*

The captivating “Social Question” of the 1870s led to a new academic discipline: “Social Policy”.¹ This trendy field soon became the favourite playground for activists, politicians and social scientists alike, paving the way for the implementation and execution of countless rigorous and enduring policy measures of the late 1880s. Although a precise conceptual definition of this extensive new area of scientific research was of no concern, Adolph Wagner among other leading scholars of the time attempted to summarize the new subject. Quite ambiguously he described it as a policy employing all means of legislation and applying the strong leverage of progressive taxation, not only to combat the “unequal and therefore unjust distribution” of income, wealth, and access to culture but also to raise the insufficient living and working conditions of the deprived masses to a socially acceptable level.² Primarily initiated in Germany by the so-called “Socialists of the Chair” under the leadership of the towering figure of Gustav von Schmoller, politically-charged terms such as “solidarity”, “social guilt” and “envy” carried the academic discussions. Socialist ideals, with central planning of educational, health care and pension systems as a means to promote a greater equality, were broadly considered functional and highly effective.³ In turn, enthusiasm increased dramatically for using the leverage of legislation to create a ‘socially just’ society and establish nationalised insurance systems. The threat of overburdening the state with more and more unappeasable demands and ungovernable tasks was conveniently pushed aside. But mention should be made here that curiously enough the same Adolph Wagner, exactly 20 years before offering his conventional, enduring and popular definition of Social Policy, had studied the dynamic growth of public obligations. In his analysis he had already discovered that the production of collective goods will cause the government’s fiscal responsibilities to spin out of control. He published those findings in 1863 and they subsequently became famous as the “Law of the Growing Expansion of Public, especially Government Expenditures”.⁴ Regretfully, during the 1880s he seems to have abandoned this insightful analysis which was an early warning against the controversial principle that, unlike in the private sphere, in the public domain the revenue collected ought to be determined by the amount of money spent.

Despite the innumerable cautious predictions by serious scholars during the past 100 or so years, advocates of social engineering and representatives of other paradigms have provided over time their sophisticated recommendations to improve the welfare state’s performance. Conceivably the concept of ‘Pareto efficiency’ became the most influential approach to welfare economics during almost all of the past century. It is probably no exaggeration to claim that a good part of modern micro-economic theory of government policy intervention in the economy is predicated on his idea. Pareto’s work also stimulated the famous debates of the 1930s over ‘market socialism’ – the chief protagonists being Dickinson and Lange on the one side and von Mises and von Hayek on the other.⁵

At any rate, it took some thirty years after Pareto’s *Manual of Political Economy* (1927) was published for the ‘new’ welfare economics to become mainstream. However, since the late 1950s the “Pareto-criterion turned out to become the integral element in the development of the idea that society faces an ‘economic problem’ – that of allocating its resources among its competing goals, in the most efficient manner”.⁶

And yet, notwithstanding countless sophisticated models based on elegant conjectures, the central intentions of the welfare state proved inadequate to explain the cultural dimension. The unintended consequences of social policy engineered to perfect the predetermined outcome thus triggered the “new social question” of our times, dominated by rising nationalism, unchecked immigration, and the apparent failure of the modern Welfare State.

What did we learn?

But what did we learn from the serious disruptions of the social fabric of advanced societies due to the ever-increasing flood of assumed entitlements? Evidently only very little!

The cultural vacuum left behind by the collapse of socialist regimes in the early 1990s was viewed once more as a convenient opportunity to perfect the welfare state with the planning tools of enlightened economists. Without much critical re-examination of the basic assumptions and without much consideration of its notoriously unintended consequences, crowds of social scientist from western states flocked into many of the so-called ‘new democracies’, seized them as laboratories for social engineering and presumptuously launched the institutions of an advanced welfare state. In a confused terminology the claim could even be heard that finally “modern capitalism” has been successfully established by decree .

However, deprived and angrily disengaged populations with a looming desire to reinstall some institutions of the old regimes are now the sobering results of an assumed public solution of a private problem.

¹ See Werner Sombart “Ideale der Sozialpolitik” in: *Archiv für Soziale Gesetzgebung und Statistik*, X, 1897.

² See Adolph Wagner, “Über soziale Finanz- und Steuerfragen”, *Archiv für soziale Gesetzgebung und Statistik*, IV. 1883.

³ Gustav von Schmoller, “Volkswirtschaft, Volkswirtschaftslehre und -methode”, in: *HdStW*, 3. ed., Vol.8.

⁴ See Adolph Wagner, *Die Ordnung des österreichischen Staatshaushaltes*, Brandstätter, Wien 1863

⁵ See FA von Hayek, “Socialist calculation. The competitive solution”, in *Economica* 7, 1940. Notwithstanding that Mises and Hayek won the theoretical argument, these debates lead to some current theories of social or economic planning and it seems somewhat indecisive whether the whole discussion had any lasting impact on the political or emotional side of the coin.

⁶ See Israel M Kirzner “Welfare Economics: A Modern Austrian Perspective” in: *Man, Economy, and Liberty. Essays in Honor of Murray N Rothbard*. W Block, Ed., L von Mises Institute, Auburn 1988.

3 *The ‘moral hazard’ of being honest*

Scarcity is a precondition of human existence and while man is prone to endless wants he is also confounded by the limited resources or means required to satisfy his desires.

Most beneficiaries of welfare favours, however, only infrequently recognize a direct link between income, taxes and government expenditures and they usually defend their ever-increasing demands on rather peculiar grounds. They act almost as if scarcity was never an issue. Moreover, they view the government as an unlimited reservoir from which benevolent politicians can appropriate funds in an altruistic manner and distribute them according to assumed rules of social justice. It is thus widely believed that the boundless number of social problems ranging from abortion and affordable housing to farm subsidies, unemployment compensation and youth programs could easily be resolved by drawing from unconstrained resources and throwing funds at them. Such actions, however, are apt to do much harm to the population’s social fabric in the long run.

Directed by rent-seeking bureaucrats and bound by finite supplies, governments cannot fulfil the fast-moving cycles of rising demand overblown by an inflation of politically advantageous promises. Individuals, groups, and multiplying coalitions of organized interests compete for social benefits or hand-outs, hereby unleashing the dynamics of greed and envy: if one person gets help or cash from the public, another is urged quickly to approach the authorities and try it too. And if one group demands higher pensions, others have to enter the competition if they do not want to fall behind. This, however, is only the rational interpretation of the game; the situation is much worse, as the most serious consequences are generally encountered in the cultural realm.

Nobody escapes the uneasy feeling that while all other groups and individuals plunder the public coffers, the government is stuck with a given number of taxpayers. As an almost automatic result the race for public funding opportunities steps up, and rent-seeking situations reveal a culturally and ethically most disturbing mechanism. It is not necessarily only greed for cash or simple envy that makes individuals ravage the budget; there are also considerations of reputation and especially peer pressure. Since only fools would hesitate to do what everybody else does, abuse of the system increases not only when it is easy to seize the money, but also when it becomes senseless and even stupid to remain honest and principled.

It is for these reasons that modern welfare-consciousness promotes rent-seeking activities by establishing new moral norms that are not much about honest social behaviour. Instead, they increasingly show us the most appropriate ways of ransacking the treasury within the framework of the law without feeling guilty or immoral.

And yet, as the welfare state like all other manmade institutions relies on firm social norms, they are neither able to sustain and strengthen them nor to promote honesty. The logic of the game thus encourages suspension of all social norms.

A comment on solidarity, redistribution, and the working of the welfare state

During the past 150 or so years the term “solidarity” underwent a thorough transformation of its meaning. Whereas the French legal expression *solidaire* characterizing the common responsibility for the total debt of families or companies was widely accepted as a vague fellow-feeling within small societies or a special form of sharing, the seductive motto “each for all, and all for each” soon raised some serious objections. Then Auguste Comte’s interpretation of the subject as “the connection of each to all others under many different aspects, so as to render the feeling of social solidarity extending to all time and in all places”¹ became the leading normative principle.

In stark opposition to this interpretation of the politically-charged term, however, Bertrand de Jouvenel labelled solidarity much more to the point as an amassed “volume of redistribution”.² The gigantic dimensions of redistribution in our times increasingly leads us, then, to perceive modern welfare states as having a high degree of “solidarity”.

Our everyday observations, however, seem to collide with the ideal of a society that accomplishes solidarity. Such a society necessarily ascribes much more importance to the opposite assumption, as material wealth goes along with the expeditious process of alienation among individuals. The most conspicuous reason for this development is the size of modern communities. The option to rely on solidarity, love, or communal spirit as mechanisms for social coordination can only be found in small face-to-face societies and the feeling disappears immediately when the growing dimensions begin to make people dissociate from each other.³

At this point formalistic mechanisms of control rapidly gaining social significance must be artificially introduced between individuals. Thus the idea of solidarity must be re-constructed and the strong face-to-face consciousness which prevails in smaller groups mutates into some sort of “welfare consciousness”. Immediate solidarity between individuals becomes somewhat romantic, and solidarity in the sense of personal cohesion begins to hide only in some remote corners, such as families, spontaneously developing support groups, neighbourhood watch systems and political demonstrations. Although protagonists of the welfare state are inclined to point to the high volume of redistribution, welfare awareness should not necessarily be viewed as a gesture for solidarity or affection. As people are induced to “unlearn” solidarity in the welfare systems, more problems are transferred to the state and remaining solidarity and individual responsibility quickly dry up. The experience that administrative help is readily available has consequences for individual political and psychological attitudes.

Although most surveys describe, and many statistics seem to prove, that there is a high level of satisfaction with the overall performance of the welfare state, people often have a peculiar and increasingly distorted understanding of their own cultural environments. Accordingly they overburden the system with all sorts of demands for better social standing, unlimited access to medical treatment, and even happiness. Most such demands cannot be fulfilled. The detrimental consequences of the welfare state are probably the results of its success and we have to make ourselves aware of how much we have already accepted of its conceptions and how much we have been brainwashed. Increasing disconnection of individuals from their own liabilities makes people unwilling and unable to provide for themselves, if the same result can be accomplished by calling on the appropriate authorities or filling out some paperwork.

We witness a crowding-out effect where public welfare projects displace and outprice established or customary initiatives. Whenever people are faced with a problem, they ask for the responsible administration or the relevant authority. By assuming that the paternalistic state ought to deal with social problems as they are discovered along the way, the subsidiary principle is put on its head. Only in the outrageous case that no programmes or subsidies are readily available do we start thinking about what we could do ourselves. However, with public support institutions at one’s fingertips the demand for all kinds of aid does not diminish; instead the desire for relief constantly increases. Thus as the welfare state produces its own overload by releasing the strain on people it cannot any longer be considered the helper of last resort – it turns out to be the helper of first choice. The split feeling, between uneasiness and total relaxation, of living in a welfare state is an expression of the fact that we have not yet adapted to the mechanisms of the large society, and we still long for the cosiness of the small and overseeable group.⁴

As success breeds rising expectations and destroys individual solidarity the need for more welfare becomes urgent. If more welfare is provided, there will be more rising expectations and less indi-

vidual solidarity. Regretfully, the success of the welfare state does not achieve its goal of making support programmes increasingly redundant – it is its efficiency and effectiveness that makes these programs indispensable and people utterly dependent. As the modern welfare state has proven its potential, its success achieves the opposite of the desired results and creates increasing number of social problems, or at least situations that are eventually defined as such. The welfare state is an institution so successful that it will never be able to achieve its aims.

Thus we face a recurring situation where the success of the welfare state is the greatest the more it fails to deliver. In order to keep people's expectations as low as possible we need an insufficiently-operating system that reveals its own helplessness.

¹ See Auguste Comte, *Cours de philosophie positive*, Paris 1830

² See especially Bertrand de Jouvenel, *The Ethics of Redistribution*, Liberty Fund, Indianapolis 1990.

³ See FA von Hayek, "The Atavism of Social Justice", in his *New Studies in Philosophy, Politics, Economics, and the History of Ideas*, London, Routledge 1978.

⁴ See FA von Hayek, "The Origins and Effects of Our Morals: A Problem for Science", in: *The Essence of Hayek*, Kurt R Leube and Chiaki Nishiyama, Eds., Hoover Press, Stanford 1984.

See also FA von Hayek "Nature v Nurture Once Again", *Encounter*, February 1971. This essay has been reprinted in his *New Studies in Philosophy, Politics, Economics, and the History of Ideas*, London, Routledge & Kegan Paul, 1978. Also Michael Zöller's *Welfare -Das amerikanische Wohlfahrtssystem*, Walter-Raymond Stiftung, Kleine Reihe, Heft 28, 1982, is of interest here.

4 Expectations always call for more interventions

The corrective state proclaims a general and exclusive competence and responsibility for most social developments. By animating their expectations it sensitises and periodically inspires population members to pursue new demands (usually at the pace of democratic elections). As people conclude that the ‘omnipotent government’¹ will take care of them from the cradle to the grave, eliminating social evils makes them even more sensitive to remaining imperfections. In turn, their rising sensitivity steadily calls for more complex state responsibilities.

If equal starting positions are not achieved in spite of all social programs and interventions, cultural frameworks must be adapted as unequal opportunities are considered ‘unjust’. Yet if we treat unequal people equally we will unintentionally put them into unequal positions. This means the only way to put unequal persons into equal positions, would be to treat them unequally. This regrettably leads to the assumption that if inequalities prevail somebody must be guilty, so government is called to action to ease inequalities by punishing the privileged through introducing confiscatory or progressive taxation systems.² Assuming that being unequal is unjust, people are encouraged to step up their demands to get even with their peers. As a result, the state is forced to provide more comprehensive health care, more national parks, bigger public universities, expanded day-care centres and more affordable housing. Starting from this principle, state interventions will eventually penetrate the whole of society, making it impossible to identify any political or cultural limit for welfare projects. If significant inequalities are assumed to be finally eliminated, smaller inequalities will quickly become a public nuisance. By creating a more comfortable environment, the welfare state increases its citizens’ sensitivity for inequalities, and long-accepted conditions will grow unacceptable.

Changing people’s morality³ makes them demand additional government projects. The implementation of equal opportunities calls for a lot of state interventions.

The paradox that enjoyment of personal freedom requires collective institutions

Individual freedom encourages people to complete their emancipation and develop their personalities. The processes of individualization create a favourable environment for unlimited personal freedom, for being left alone, as well as for unrestricted democratic systems. At the same time, however, these processes dissolve almost all social connections. Family bonds are loosened and naturally-evolved living conditions in communities, small towns and regions rapidly vanish. As the homogeneous background in agricultural, aristocratic, bourgeois or proletarian environments dissolves before our eyes, we witness the erosion of the family as the all-important core of any social integration. But without the functioning family nucleus, which among many other purposes serves as the decisive meeting place for family members, the necessary altruistic care will no longer be provided.⁴

Owing to the excessive tax burden, it is not unusual that both parents are forced to work in order to provide for a decent living and an adequate lifestyle. As a result, small children are kept in public or private day-care centres and schoolchildren are mostly viewed as a burden when they return from school earlier than mid-afternoon.

Affluent societies may be inclined to fulfil most rational desires of their members, but these developments require collective welfare institutions to take over the former “household production”. But this is not a matter of incentives alone. Today’s dominant icon, the skilled, highly specialized, and dynamic urban individual, is no longer suited for activities such as caring, nursing or raising children in a meaningful way. Today’s successful personality is chiefly shaped by rationally calculating egocentrism fed by the imperatives of the prevailing system. People tend to transfer their own burden to public budgets because they think such a move can improve their own financial situation. For

many, at least, it seems the best way to recover from the state what they conceive as their entitlement. In countries with less-developed welfare systems people have to work harder and earn more money to buy services in the open market. If, however, in the process of individualization only a few groups and communities are left that are able to provide the necessary services, the individualized society has to built up more collective institutions – hospitals, kindergartens, foster homes, schools and retirement centres – to take over these essential functions of small groups.

A dense, interdependent and interwoven bureaucratic system with its forces of rationalization still leaves some leeway for free individualistic behaviour, whereby extravagant and egotistic people can spontaneously develop some sort of split self. But advanced societies are becoming more rational and more hedonistic at the same time. On the one hand we want to achieve social conditions of total relaxation, permanent well-being and an everlasting condition of happiness. Modern welfare societies are thus characterized by emotional arousal, showing a tendency to rid themselves of any annoying obligations that would unavoidably prevent one's emancipation and impede the everyday life of their members.

On the other hand, acting spontaneously today requires smoothly-working collective institutions which remove many of these impediments from our shoulders as routine obligations are transferred to the welfare state or other comparable providers. Nobody is willing and able to take care of the elderly and needy members of society anymore, so they will be put into a subsidized retirement centre. And because of the existence of many caring institutions we experience strong cultural support for spontaneous and even deviant life styles.⁵ Here again is a paradoxical combination of tendencies: rising hedonism, spontaneity and living for the moment, versus rising demands for more security and dependability.

Our freedom and independent lifestyles, the virtues of spontaneity, and our high mobility depend increasingly on collective institutions and require collective planning. Although we appreciate individualistic emancipation, it nevertheless seems to be instrumental in breaking down private welfare services such as education for the young and care for the sick, old, and poor.

We create more risks by the sheer attempt to eliminate them

As people think they can rely on the paternalistic welfare state's duty to look after them and protect them from hardship, even the countless minor risks with which individuals could easily cope have become a public matter. It is also widely believed that central governments should tackle new risks such as nuclear power, the greenhouse effect, bio-technology and gene manipulation, so people are increasingly unwilling to accept moral responsibility and cope with life's risks. As a result we are administered by a myriad of regulations which constrain our daily actions. Although most of these measures seem reasonable they completely oppose free-market principles. The dream of a risk-free society creates yet another paradoxical consequence: the more the state tries to reduce or eliminate risks, the more we become incapable of even grasping them.

The argument at this point, however, does not imply that people wish to transfer the responsibility for all kinds of hazards to the state. Much worse – they are becoming increasingly unfit to recognize them, let alone to respond in the appropriate fashion to the ethical questions of our time. While governments are busy tackling or abolishing most risks, new social hazards are discovered faster than they can be removed. This vicious circle fosters cultural tendencies making the family structurally and financially unsuited to sustain traditional social bonds and services and provide support and care.

Thus the machinery of the welfare state with its fairly dependable infrastructure, monthly paychecks, and presumably inexhaustible resources is viewed as the only reliable helper and stable fixture in society, while the world of individual freedom and free enterprise is getting riskier all the

time. We observe a slowly-spreading culture where people get used to putting more trust in the welfare state's bureaucracy than in the dependability of their own relatives and friends. Hence, by necessity, the state adopts the paternal role of "Big Brother".

We have to conclude that the more individualized, emancipated and autonomous the circumstances are in which individuals are living, the more they tend to develop this welfare-oriented attitude and increasingly depend on collective institutions. The daydream of living in a risk-free society turns out to be a very risky gamble.

Preventive vs. corrective welfare state?

The task of the welfare state is to improve conditions that are presumed as socially unacceptable, but collective settlement of social problems by force or subsidies may still not be the most expedient way to deal with them. As prior prevention of undesired social developments often proves much more reasonable and efficient than most subsequent correction, the refined welfare administrations of advanced states are increasingly compelled to conduct even more comprehensive control of their citizens. Unlike law that not only punishes wrongdoing but also impedes delinquencies, enforced prevention of human actions by the authorities replaces civil rights with a gamble on guaranteed security. People are forced into compliance and standardized pragmatic behaviour by the inherent logic of collective action: individualists, off-centre artists or harmless nonconformists are gradually pushed aside or even rejected. This, however, has far-reaching cultural and political consequences – the traditional corrective-therapeutic welfare state has to identify existing problems to justify social interventions, but the more sophisticated prior-preventive welfare state has to ascertain the identity of conjectural or dormant social problems in order to unleash its might and political means.

Countless surveys are conducted and people are coerced to fill out forms where they state under the threat of penalties what they think that they think, but most of these collected and computed figures are useless as they cannot reflect the dynamics of markets and culture. Statistical data compiled with state-of-the-art technologies will never reveal the working of the inner fabric of societies and the many nuances of a community's conscience. Ordinary citizens are usually left helplessly exposed to overpowering information about collective needs and urgent public programs, while the state machinery gains an unrestrained dynamic. For political reasons the preventive state often starts its intended intervention prior to its democratic resolution. Budgetary problems and the adoption of undemocratic measures usually follow. Attempts to censor the press, surveillance cameras, spying on fellow countrymen, prohibitively high inheritance taxes, mandatory social security contributions, enforced union dues and collective instructional programs are but a few examples. When the risks and hazards of our lives are removed before they are even experienced, the state's enlightened paternalism eliminates individual freedom and creates another paradoxical situation.

Any reasonable-sounding strategy to foster prevention instead of simple repair is the greatest threat to a liberal (in the European sense) society. Where most things are always safe, no freedom can exist.⁶ Thus the inefficient welfare state is more democratic, and allows us more individual liberty, than the efficient welfare state.

Anticipating benefits generates selfishness

Advanced welfare states take pride in redeeming a rational perspective of evaluating the overall costs of individual decisions; at the same time they neglect important but intangible social values such as merit, due or reward. Yet as our welfare consciousness is shaped by rationality that fosters the elimination of market forces, people still maintain the calculating perspective of markets as an innate and shared feeling. More and more smart ways develop to claim handsome benefits and appropriate lucrative subsidies. This suggests that citizens as well as non-citizens carefully assess their entitlements and compute their chances to extract maximum benefits from the state. Situations are often faked to capitalize on any legal or semi-legal opportunity to exploit the collective system. The

rational welfare society has made all kinds of income transfer socially acceptable by successfully removing feelings of disgrace and guilty discomfort from handout-recipients and those who remain on welfare. Degrading lines outside the welfare office are long-gone memories. Most of us receive some kind of welfare benefits so nobody can be accused of living off the charity of others. This enforced ‘de-stigmatisation’ of receiving public support encourages an unfettered computation of prospective benefits. If one wants to get all benefits as a student, one decides to stay longer in school. If one wants a larger donation from the state, one postpones marriage for a certain time and plans babies’ the birthdays around the availability of child support.

The exact calculability of benefits and transfers is just one example of the welfare state’s many unintended consequences. Yet it explains why there will never be much progress in eliminating poverty, and why there will never be enough public universities, and why the pay-as-you-go pension systems are doomed.

The contraction of “real poverty” and the implementation of “basic medical care” (whatever this might mean) for all in most countries must be viewed as a positive effect of the welfare state. Yet these achievements have behavioural consequences and again create a paradoxical combination of tendencies. Providing the means to make people independent, and promoting a new and mostly unfamiliar lifestyle, aggravates the original problem. The odium of being on welfare has been eliminated, but a growing tendency to calculate benefits is the unwanted consequence. The welfare state makes unpleasant social situations more attractive and opens up new opportunities which undermine its own goals.

¹ This is the title of one of L von Mises’ rather neglected books: *Omnipotent Government: The Rise of the Total State and Total War*, Springsmill, Penn. 1944. Influenced by the circumstances of the time and dealing with the consequences of war, this work contains many important insights.

² Although the history of progressive taxation can be easily traced from our current sobering experiences to the Florence of the Medici back to the Greeks, it has always been viewed as unjust. See Edwin RA Seligman, *Progressive Taxation in Theory and Praxis*, 2nd. ed., Baltimore 1908. Of special interest are the two mentioned ‘discorsi’ by Fr. Guicciardini, who vehemently rejected progressive taxation.

³ Christian Bay’s book *The Structure of Freedom*, Stanford, Stanford University Press 1970 is of interest here.

⁴ On this point see especially Gary S Becker’s illuminating book, *A Treatise of the Family*, Chicago, University of Chicago Press 1991.

⁵ See Michael Zöller, “Wissen und Handeln oder warum Ordnung möglich ist”, in: *Vordenker einer neuen Wirtschaftspolitik. Festschrift für Christian Watrin*. The International Library of Austrian Economics, KR Leube, Ed. Vol.5, FAZ Buch, Frankfurt 2000.

⁶ See especially chapter 17 of FA von Hayek, *The Constitution of Liberty*, The University of Chicago Press, Chicago 1960.

5 *Concluding suggestions*

Many view free markets as incompatible with all kinds of social problems, and with the protection of the environment and agriculture, to mention but a few hot issues. For them the very notion of market solutions for pension funds, environmentalism, or the privatisation of health care systems or universities represents an oxymoron. Even many “free marketeers” find themselves on opposite sides of the fence when it comes to governmental regulation and state interventions in these sensitive areas. Most are convinced that markets work best to allocate the goods and services we enjoy, but argue that social issues are different and much too precious to be allocated on the basis of demand and supply.

Although questions of principle, these disputes do not necessarily mean that there is no proper role for the government to play in these sensitive fields. But government’s involvement ought to be confined chiefly to three tasks: first to continuously improve the legal framework and institutions needed to make the market function more effectively, secondly to induce individuals to take more account of the effects of their actions, and finally to act as agent of the people in circumstances where governments render specific information which could not be provided by the market. It should, however, be emphasized that government should not be granted an exclusive right to supply these services but should be legally obliged to encourage development of private alternatives.

The complexity and incomprehensibility of the current social security systems represent a positive danger for democracies. These covert redistribution systems are to some extent to blame for transforming market societies into some sort of mixed economies. The dispute about what, when and how much should be given to those in need owing to circumstances beyond their control persists and keeps dividing the population, but the entire setup should be gradually changed from a collective to an individualized system. To initiate such major modifications it seems reasonable that government should help to develop suitable independent institutions. Thus, for a time period defined and enforced by democratic vote, the state should require all citizens to make provisions which will prevent them from becoming a charge on the public purse. Regarding old age and health provisions, poverty and unemployment we should proceed in the same way that we require car owners to get insurance against third-party risks, not in their own interest but in the interest of others who might be injured by their actions. Designed by Jose Pinera, the system of private pension funds was successfully introduced in Chile in 1981.¹ Since then this capital-accumulation system has replaced the financially unaffordable pay-as-you-go system in a number of countries. Yet it is an odd fact that the countries with the most bankrupt pension systems are the most hesitant to consider adopting this successful alternative.

The prevailing view that markets and the environment do not mix is bolstered by the perception that resource-exploitation and environmental degradation are linked to economic growth. This conception, however, could be reversed by gradually introducing and applying market principles to protect the environment and sell state-owned assets. Free-market environmentalism does not suggest that there is no role for government;² on the contrary, this approach presupposes well-specified property rights to enable action with respect to all kinds of natural resources. The abuse of our air as a collectively-used factor of production, for example, is more of a problem than solid waste disposal in the ground, because property rights to the earth’s surface are better defined than those to the atmosphere. While private ownership of land works very well for producing wine or wheat, the measuring, monitoring and marketing of land for the habitat of endangered species is still considered an obscure idea.

Definition and democratic implementation of enforceable property laws will remain a domain of the state for the time being, requiring a firm legal framework, entrepreneurial skills, and a lot of educational efforts that should already start in elementary schools. Whether property rights are held by

individuals, corporations, or non-profit and communal groups, powerful control is always imposed on resource-users because the wealth of the owner of the property right is at stake if bad decisions are made. Of course, the further a decision maker is removed from this disciplining control – as is the case when there is political control – the less likely it is that good resource stewardship will result. Moreover, if well-specified property rights are transferable, owners have to consider not only their own values but also the decisions of others and how much they are willing to pay.

In those rare cases where rights cannot be measured, monitored or marketed there is of course only a slim prospect for a market exchange. For example, where there is water pollution from sources that cannot be identified with current technology at reasonable costs, defining and enforcing property rights governing water-use may be difficult or even impossible. Likewise, excluding non-payers from enjoying a scenic view may prove so costly that a market situation may not emerge under present circumstances and institutions. Such cases can only be perceived as remote, but government interventions could be considered to support development of market conditions with decisive and imputable property rights.

Results from centrally-planned resource allocation will never work better than markets; we have nevertheless developed the tools to distinguish chiefly between two types of government interventions. “Adjusting” interventions can be compatible with free markets if their time frame is properly defined, well administered, and firmly enforced – such programmes seek to support people, groups or institutions needing help owing to circumstances beyond their control. “Preserving” interventions, aiming to preserve the status quo, however, are under known circumstances absolutely incompatible with the very nature of markets.³

¹ See especially Jose Pinera’s pathbreaking book *El Cascabel al Gato*, published in 1991 in Santiago/Chile. This slim book was revised in 1995 and was published in Madrid as *Sin Miedo al Futuro* (1995) with a preface by Pedro Schwartz. In the meantime it has been translated into several other languages, among them German and Polish. This book should be used as an instructional guide to privatise social security systems worldwide.

² See especially Terry L Anderson (DL Leal co-author) *Free Market Environmentalism*, Cato Institute, Washington 1993. Anderson is among the leading scholars in the field of free market environmentalism. His *Breaking the Environmental Policy Gridlock*, Stanford, Hoover Institution Press, 1997 is also an important contribution to the public debate over the proper role of government in managing natural resources and market incentives to spur conservation and protection of the environment.

³ An enlightening discussion of the concept of ‘interventions’ is to be found in Ludwig von Mises’ *Nationalökonomie. Theorie des Handelns und Wirtschaftens* (Geneva, 1940, second ed. 1980). A new facsimile edition has been published recently by Verlag Wirtschaft und Finanz in Düsseldorf. This is the most important German forerunner of his *Human Action* (1949). Regretfully, due to the circumstances of time and place, this magnum opus was completely neglected and no longer reached the public.