

Paradox of thrift

<https://www.taxresearch.org.uk/Blog/2025/12/09/paradox-of-thrift/>

Published: January 12, 2026, 8:30 pm

Having mentioned the economic concept of the paradox of thrift [in a post this morning](#), I realised there was no glossary entry on the subject, so I drafted this:

Paradox of thrift

The paradox of thrift is the idea, first popularised by John Maynard Keynes, that although saving more might make sense for an individual household wanting greater financial security, if everyone in the economy tries to save more at the same time, the consequence can be a collapse in overall economic activity that leaves society worse off.

The logic is straightforward.

First, every person's spending is someone else's income.

Second, when fear, uncertainty or economic shock encourages households and businesses to cut consumption and investment, total demand in the economy falls.

Third, the resulting decline in sales forces businesses to cut production, wages and employment.

Fourth, as a result, national income falls, and the very savings people hoped to increase become harder to achieve because there is less income from which to save.

The paradox of thrift does, therefore, show that individual rational behaviour can lead to collective harm. This is the so-called fallacy of composition at work. What is wise for one household is not, when aggregated, good for society.

This insight matters profoundly for public policy. When private saving rises and demand collapses, only the government can step in to spend, sustain incomes, maintain

employment, and prevent recession. Austerity in such conditions, of the sort, for example, imposed in the UK after 2010, is therefore the exact opposite of what is required. It compounds the paradox: government cuts reduce spending still further, deepening the downturn and undermining the well-being of the very households urged to “live within their means”.

In short, the paradox of thrift explains why a healthy economy requires both confidence and spending, and why governments that can create the money we need should never be afraid to use that capacity to sustain prosperity when private actors retreat.

Comments

When commenting, please take note of this blog’s comment policy, [which is available here](#). ***Contravening this policy will result in comments being deleted before or after initial publication at the editor’s sole discretion and without explanation being required or offered.***