

# Why local money flows matter

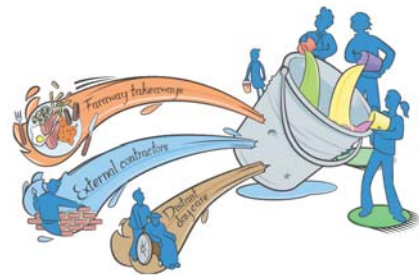
## Promoting local economic linkages

For many years, the proposed solution for regenerating urban and rural areas has been to attract more money into them, whether it is in the form of tourism, agriculture, corporate relocations, and other forms of inward investment. There is, however, a different approach that can have an even greater, more sustainable, impact: regenerating the local economy from within by taking advantage of the resources that a community already possesses.

## The leaky bucket

In many areas, the issue is not that too little money comes in but that most of the money that does enter the local economy flows right out again in the form of spending on and contracts to non-local businesses and labour.

The local economy looks a lot like a leaky bucket. Money enters the way we pour water into a bucket. But a lot of that water leaks out of the bucket, just as we spend money on external services. Leaking is not innately bad because economies are connected, and this exchange of money promotes innovation and cultural exchange.

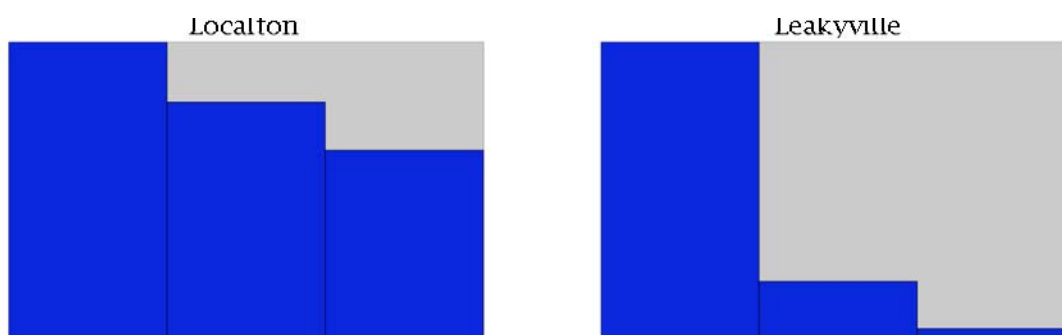


In communities facing economic disadvantage, however, there are two ways to increase the circulation of money: pour more water into the bucket or find ways to 'plug the leaks'. Plugging the leaks by creating economic linkages in poorer communities between local businesses, labour, and public bodies can build a healthy local economy that can stand on its own long after regeneration funding dries up.

## The multiplier effect

There is a way to measure just how much the water flowing into your bucket circulates around before leaking out, and it's called the multiplier effect. This name comes from the understanding that money entering an economy has a multiplied impact the more it circulates.

Take two imaginary local economies: Localton and Leakyville. In Localton, everyone magically spends 80 percent of his/her income locally. That means if someone receives £100, she spends £80 locally on a service, that person spends £64 locally, and so on. In Leakyville, where everyone magically spends 20 percent of his/her income locally, that same £100 circulates differently. So £20 is spent on the next person, then £4, and so on. The areas in blue in the charts below depict the multiplier effect, and the different amount of income generated in Localton versus Leakyville.



## **Plugging the leaks**

Plugging the Leaks is an action-planning tool, based around a one-day workshop, which enables people to explore together how their local economy works and to develop ideas for improving it.

Residents, the public sector and businesses cannot revitalise the local economy alone. Most creative solutions involve people working together. Plugging the Leaks brings everyone to a workshop setting to explore their local economy with the use of simple visual images. The Plugging the Leaks process explores how money enters an area, how it leaks out, and what action will plug those leaks. The result is a simple tool that shows everyone how to strengthen the local economy and how to take action for lasting change.

## **Local Multiplier 3 (LM3)**

Local Multiplier 3 (LM3) is a tool developed by nef (the new economics foundation), based on the multiplier effect, to help all members of a community understand and take action around local money flows. LM3 enables organisations to measure the impact they have on a local economy by tracking where the money they receive is then spent and re-spent. The purpose of tracking and measuring this spending is to identify opportunities to get more money circulating locally. Economically disadvantaged communities can achieve more local circulation of money by strengthening linkages in their local economies.

LM3 works like this:

- 1) Measure an organisation's income, which may be a combination of public and private funds (Round 1);
- 2) Then look at how that organisation spends its income and how much goes into a defined local area (e.g. parish, ward, district, or 30 mile radius) - suppliers, staff, subcontractors, and overhead are typically the principal expenditures (Round 2);
- 3) Then look at how the people and businesses who received money from that organisation - the suppliers, staff, etc. - spend their money (Round 3);
- 4) Finally, run through some quick maths to arrive at the LM3, which tells you how much spending by the organisation impacts the local economy.

In many cases, people find that they can spend less money to generate more income for the local economy! It's not just a matter of how much money you spend but how you spend it.

## **Who is using LM3 now and how?**

### **Voluntary Sector**

In order to make it possible for a much wider range of organisations to use LM3 the model is now available free of charge online for not for profits. For example at the moment four organisations in Tyne and Wear are using the model as part of a broader process in demonstrating the value of the sector to the local economy. In Camden the council is working with the voluntary sector to help them benchmark their contribution in areas as part of an Invest to Save bid.

### **Public Sector**

LM3 is being used by over 20 councils in the North East to assess their contributions to the economy. Recent work (not yet published) commissioned by the RDA has used the approach together with the Durham Business School model to look strategically at the value of all public procurement in the North East Economy.

### **Private Sector**

One of the major utility companies is currently using the private sector model across a range of projects. A number of other companies are now using the methodology to inform their CSR programmes. A further program is just starting looking at the application in multi-national business.

## **More information**

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You can download a powerpoint demonstration of how LM3 online works from here: <http://www.adamwilkinson.com/downloads.php>

You can find more information on:

[www.lm3online.org](http://www.lm3online.org)

[www.neweconomics.org](http://www.neweconomics.org).

[www.adamwilkinson.com](http://www.adamwilkinson.com)