Buying Local and the Mythical Multiplier of Seven

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If you hear the same thing from different people over and over, after awhile it is likely you will accept it as fact. It is taken as an article of faith in community business circles that money spent locally reproduces like frisky bunnies. People will state with solemn certainty that a dollar spent on main street "turns over" seven times, implying that a locally spent dollar blossoms into $7.00 in the area economy once everything is said and done.

Wouldn't that be neat if true? It's not, it never has been, and the distortion is getting worse as the years go on and as small town boosters strain to promote their economies and entice locals to buy locally instead of visiting those big-box stores over yonder.

Here are some recent claims of a local multiplier of 7.0 in the promotion of local initiatives:

> One mid-Iowa community mounted a buy-local campaign last year and used a 7.0 multiplier to assert a potential local total sales gain of $11.4 million from the effort.
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> In its presentation petitioning the Iowa Legislature to help underwrite the development of a local amenity, another community concluded, after using a multiplier of 7.0, the project would boost the local economy by $120 million.
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> A retail loan fund was set-up in a northern Iowa community, and the local news story announcing the program matter-of-factly asserted that "each dollar spent in retail is turned over an estimated seven times."
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> A downtown retailer profiled in a major Iowa trade publication last year chimed: "Money spent in towns turns over seven times when purchasing locally."
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> A Mississippi River community's official city web site currently states that "tourism dollars turn over within the local economy seven times."
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> And finally, one community exhorts us to "please remember to shop [local] merchants. Economists tell us each dollar spent turns over seven times."

Goodness, wouldn't you like to get some of that action? How such an uncritically-evaluated assumption gained such momentum and so widely is perplexing.

Consider this. I go to my locally-owned furniture store and buy a lamp for $100. Unless that lamp was made locally, and odds are really high it wasn't, half or more of that purchase price immediately must leave the economy to pay the wholesaler, the truckers, and the original manufacturer. With what's left, the shopkeeper must pay all operating costs and her workers, who in turn buy things both inside and outside of that local economy. Lickety-split, most of that $100 is no longer here.

When I add it all together using the standard economic impact models of Iowa's trade areas that I maintain at ISU, and after taking into account all of the rounds of spending by all of the affected parties, I typically find that a dollar spent locally on retail goods or services results in from $.25 to $.40 in additional economic output in the region. So the multipliers I would use to describe the localized economic value of increased local cash-register purchases would be in the range of from 1.25 to 1.40 depending on the size and complexity of the regional economy. Small economies have lower multipliers, and larger economies have bigger multipliers, but not that much bigger.

The perplexing question is how you go from an economist-derived multiplier ranging from 1.25 to 1.40 to a cock-certain value of 7.0 when you are talking to someone downtown? I suspect that people have confused the physical movement of money through a local economy – how many times a dollar literally changes hands – with how much money is actually retained within a local economy. A dollar can change hands an infinite number of times, but the physical movement of a particular dollar is not a multiplier.

Using an impact model of a medium-sized, northern Iowa county that serves as a regional trade center, let's say that over a month I spend $200 each on a furniture item, groceries, sporting goods, clothing, and dining out for a grand total of $1,000 in local spending. After all transactions are accounted in the model, my initial $1,000 of spending would have created only an additional $273 more regional output, not $6,000 more as the wistful boosters would have you believe.

Stated differently, and in a manner that makes much more sense in terms of understanding economic impacts, each million of cash-register sales like I just described supports annually 14 jobs and $286,000 of incomes to workers and shopkeepers in that economy.

There are "multiple" offenders out there, but the most egregious of the lot of late are among the buy-local boosters, including local foods advocates. I have done many buy-local studies for Iowa's communities and interests over the past 20 years. The actual multipliers are knowable, reasonable, and … low.

Still, wouldn't it be cool if money really did breed like bunnies?