



# Downtown Economics

Ideas for Increasing Vitality in Community Business Districts

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## Importance of Buying Local

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A growing body of evidence suggests that the businesses most beneficial to a community are those that are independent and locally owned. This article provides an introduction to the potential economic, social, and environmental benefits provided by local business.

### Economics

Perhaps the most compelling reason to buy local and independent is economics. Some studies from across the U.S. conclude that spending a dollar at an independent business generates about three times as much benefit to the local economy as spending a dollar at a chain or discount retailer<sup>1</sup>. The reason is that chains pull money out of the community to support expansion, offices, and profit to the home office (and staff) located elsewhere, while local businesses spend more of their revenue buying goods and services from other local businesses.

Big-box stores are built upon the model of replicability, low prices, and economy of scale. However, one study suggests that shopping at Wal-Mart does not always save consumers money<sup>2</sup>, and a second found that product prices were not compellingly lower (1.5 – 6%) on comparable product options<sup>3</sup>.

### Economic “Leakage”

Buying local does not “create more money.” Rather, it prevents money from leaving the community, referred to as “leakage.” Why is leakage important? Leakage means value lost to the community to other locations, rather than reused and reinvested locally. A *leakage analysis* can be completed to illustrate particular sectors of the local economy that may be underperforming and allowing capital to be lost. Through the careful application of leakage analysis, a community can identify goods and services being imported to the community that could be produced locally and focus public and private efforts accordingly. A solution is to support and prioritize the growth and expansion of locally owned businesses that specialize in offering local and domestic products. It is important to note that promoting local businesses and products does not mean cutting off the community from the global economy.

This principle goes beyond retail to consumer and business services. Completing personal or business banking and financial services through a national bank, even if it is a local bricks-and-mortar branch, causes leakage back to the parent company. Supporting locally owned banks or credit unions is one way to reduce economic leakage in a community.

Encouraging and educating local business and consumers about the benefits of doing their business locally by seeking local business services and maximizing local business-to-business transactions is a key strategy for buy local efforts.

Beware the easy solution - introducing chain retailers into a community introduces hidden leakage. Basic retail trade leakage analysis may suggest holes in particular retail sectors. The knee-jerk reaction is to plug that hole, even if it is with a chain. While sales occur at the chain, perhaps closing surface-level holes in the local retail landscape, that chain pulls money out of that market while a local establishment would create greater recycling and reinvestment of monies locally. A more accurate assessment of leakage would view sales at chain retailers as siphoning a portion of their sales out of that market.

Some longitudinal studies suggest that after the arrival of a major discount retailer, there is a short-term increase in county-level retail employment, but the long-term net result is job loss in the retail sector<sup>4</sup>. In the process of supporting their supply chain and other corporate activities, the discount retailer draws sales and jobs from pre-existing retail businesses in their affected market area, resulting in a total net loss in jobs and money circulating in the local economy.



A 2008 study by Civic Economics suggested that if the 600,000 residents of the Grand Rapids, MI region replaced 10% of their purchasing with local businesses, it would create an estimated \$140 million in new activity and support 1,600 jobs from \$53.3 million in wages in the trade area<sup>5</sup>. This increased activity is due to the capture of lost capital and “economic multiplier” effect - the reinvestment and cycling of capital within the local market.

### **Economic Stability**

Independent retailers and service providers are typically less tied to the national and global economy as their chain counterparts. This may be somewhat of a disadvantage during times of economic prosperity, yet may be an advantage during hard economic times and uncertainty. Having a robust diversity of locally owned businesses may provide some insulation from broader market fluctuations<sup>6</sup>. This may be due to maneuverability and innovation of small firms<sup>6</sup>; or from a strong network of local and independent businesses creating a mutually beneficial self-reliance and resiliency that reduces the export of capital from community- building wealth locally. A diverse base of local businesses across sectors is also critically important should particular areas of the economy falter.

### **Quality**

A series of Consumer Reports studies found that independent drugstores outranked all other pharmacies in providing personal attention, service, customer satisfaction, and selection without missing the mark on price. Independent pharmacies have topped every Consumer Reports survey since 1998.<sup>7</sup> Locally owned and independent businesses do not intrinsically provide a higher quality product than do chains on the basis of ownership. However, locally owned businesses are often more connected to their market and are responsive, and thus must offer a high quality product and service to compete with chain and discount retailers.

### **Social Connection**

A study from the University of California-Davis followed people around as they shopped in a supermarket and found that chances of a customer having a conversation with another shopper are about 1 in 10. They then tracked people at farmers markets and found that the odds of having a conversation there are nearly 70 percent<sup>8</sup>.

Locally owned businesses tend to be more active and attentive to local issues and business organizations, fostering a collaborative sense of community, as opposed to the often “face-less” corporate chain. Communities often hear more about donations from large businesses – because they often come in lump sums and widely publicize their efforts. However, it may be more consistent and generous support from local businesses that keep the doors of charitable organizations open. A study of businesses in Oregon found that small businesses donate about twice as much per employee to charitable organizations as large businesses<sup>9</sup>.

Locally owned businesses tend to not relocate frequently, thus there is less vulnerability to the community to invest locally. These businesses also drive entrepreneurship and creativity, fostering one-of-a-kind businesses and those with distinctive character.

### **Environmental Benefits**

The local environmental benefit of buying local may be difficult to quantify. Importing fewer products to the community and shorter supply chains may reduce oil use and air pollution. Local businesses are also far more likely than chains to stock local and regional products, supporting other local businesses and shortening supply chains. Businesses located in walkable settings are more likely to be locally owned, reducing local traffic and emissions. The impacts of products produced locally, such as food, are visible to consumers, enabling greater accountability. Local businesses may be more likely to restore existing and historic buildings, and invest in local infrastructure than chain counterparts.

### **Conclusion**

Today’s consumers are well served by national retailers and e-commerce sellers who have replaced many of our local stores. However, there are many economic, social and environmental benefits resulting from supporting local businesses. Accordingly, the incremental benefits of buy local programs should be considered when establishing a comprehensive downtown economic development plan.

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<sup>1</sup> See Civic Economics, “Thinking Outside the Box: A Report on Independent Merchants and the Local Economy,” September 2009; Civic Economics, “The San Francisco Retail Diversity Study,” May 2007; and Institute for Local Self-Reliance, “The Economic Impact of Locally Owned Businesses vs. Chains: A Case Study in Midcoast Maine,” Sept. 2003.  
<sup>2</sup> Bernstein, J., Bivens, J., & Dube, A. 2006. “Wrestling with Wal-Mart: Tradeoffs between Profits, Prices, and Wages”. Economic Policy Institute, June 15, 2006  
<sup>3</sup> Basker, E. 2005. “Selling a Cheaper Mousetrap: Wal-Mart’s Effect on Retail Prices.” *Journal of Urban Economics*, Vol. 58, No. 2.  
<sup>4</sup> Neumark, D., Zhang, J., & Ciccarella, S. 2007. “The Effects of Wal-Mart on Local Labor Markets”. Public Policy Institute of California, IZA Discussion Paper No. 2545.; Basker, E. 2005. “Job Creation or Destruction? Labor-Market Effects of Wal-Mart Expansion”. *Review of Economics and Statistics*, Vol. 87, No. 1.  
<sup>5</sup> Civic Economics. 2008. “Local Works! Examining the Impact of Local Business on the Western Michigan Economy.”  
<sup>6</sup> Mallett, T. 2010. “A Peek at the Trough: Small business employment outperforms mid-sized and large firms through recession.” Canadian Federation of Independent Businesses.  
<sup>7</sup> Consumer Reports: “Time to Switch Drugstores?” October 2003; “Drugstore comparison: Which store is best for you?” June 2008; “10 Ways to Reduce Your Drug Costs.” March 2009.  
<sup>8</sup> Robert Sommer, John Herrick, and Ted R. Sommer, “The Behavioral Ecology of Supermarkets and Farmers’ Markets,” *Journal of Environmental Psychology*, (1981) 1, 13-19.  
<sup>9</sup> Friskhoff, P. 1991. “Business Contributions to Community Service”. U.S. Small Business Administration.

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