1. Why the usual approaches to economic development aren't working

'The problem is not necessarily that too little money flows into a neighbourhood. Rather it is what consumers, public services and businesses do with that money. Too often it is spent on services with no local presence, and so immediately leaves the area.'

The Government's National Strategy for Neighbourhood Renewal[1]

It can seem obvious – a basic economic fact of life – that if an area is poor, it needs money poured into it. This might be by attracting in inward investment that will create new jobs; a regeneration grant to develop local infrastructure; or building tourist attractions that will have people flocking in. Everyone assumes that money will improve the area, eventually 'trickling down' to reach those who need it most. But does it?

Canning Town has experienced every state-sponsored regeneration initiative since the 1960s[2]. Yet it is still home to one of the most extensive areas of urban deprivation in Europe. Government schemes, such as New Deal for Communities, are bringing in over £50 million to each recipient area. This is a huge amount of money. And in really poor communities, benefit payments alone will add up to twenty times as much as the New Deal. So why is it that these colossal sums of money are not alleviating poverty?

The answer lies at two levels. First, how much of the money actually makes it to the local economy in the first place: how much is instead deposited into the hands of external consultants or contractors? Second, how hard does that money work? In other words, how many times it is re-spent locally before it finally leaks away.

The problem is that pouring money into an area has minimum long-term impact if the wealth flows straight out again because there is nothing to hold it in the area.

Economic development experts have historically spent much of their time attracting large businesses into poorer areas in the hope that they will employ some local people. This could take the form of a Japanese car manufacturer or a call centre. Usually some local jobs are created, with varying levels of quality. However there are several challenges to the inward investment approach:

1. Because so many local authorities in the UK and abroad are competing for such investment, they have to offer enormous incentives, which can offset any benefits. One recent study in London showed that the collective incentives added up to more than the benefits brought when the company finally relocated
2. If a company can be attracted to your area, it can often be attracted out of it if better incentives are then offered elsewhere. This is exactly what happened when Dyson suddenly announced that they were moving from Gloucestershire to Malaysia

3. It's a 'one size fits all' approach, not very sensitive to local needs and resources. One software company coaxed into relocating to the South Bronx in New York found, surprise surprise, that it couldn't recruit enough local software 'coder-writers'
4. Unfortunately, as with regeneration funding, simply getting the investment into the area isn't enough. It is the linkages that that investment can make with local firms and local people that determine whether or not local people are in fact any better off. Many assume that such linkages will occur naturally, however a case study of a Toyota plant found that only five out of 240 companies providing inputs were from the region; and a Scottish electronics companies study identified only 12% of material inputs as being from Scotland[3].

This issue of developing local linkages is very important, yet it is a process that is often not supported as effectively as it could be. Experts can help, as North East Lincolnshire's Buy Local programme found. But it is a process that cannot be undertaken by the 'experts' alone. Local people, businesses and other public sector budget-holders hold the keys to many of these connections. And it is only if an inward investment is really embedded, with a thick web of local linkages and ties, that it can secure a long-term future.

The same holds true for other in-flows of funding – be it tourism income, agricultural sales, welfare benefits, or grants. All too frequently, little of this money reaches the hands of local people, and that trickle leaves the area again far too quickly.

So – what does this mean in practical terms? What can the many developing partnerships between the public sector, private sector and community actually do to improve their local economies? This is a particularly important question for time-limited regeneration initiatives – because at the end of the funding period, when money is no longer pouring into the economy, what will matter most is what is stopping that money from leaking out.

We need to start making all the money that enters a poor community work much harder than it currently does. This handbook shows you how.

2. Leaving it to chance

'The corner shop is the elephant of the local economy.'

Participant at a leaky bucket workshop hosted by the National Council of Voluntary Organisations

Most economists these days argue that the most 'efficient' economy will naturally be created if we allow market forces to prevail. But does the evidence actually support this view? And does 'efficiency' meet your community's needs?

5. The leaky bucket

'Plugging the Leaks has given me a much clearer understanding of the local economy. Both the ideas and the process of bringing lots of different groups together will feed into the local authorities' community strategy.'

Glen Parker, South Staffordshire District Council

So what is this leaky bucket that Jackie Gill, Glen Parker and many others have found so helpful? The scientist Francis Bacon said four hundred years ago that money was like manure: 'no use unless it is spread'. Maybe so, but we find it is easier to talk about money as if it were water.

Imagine the local economy as a bucket. Nothing fancy or complicated; just an ordinary bucket like the one under the kitchen sink. If someone has £5 and spends it in the local grocers, the £5 stays in the bucket. But when they pay the electricity bill, it doesn't stay in the bucket. Spending on electricity is like a leak in the bucket: the fiver leaks out as the supplier is a business outside the area. But there are usually ways of stopping all of the five pounds from leaking out. Insulating the house will cut the electricity bill, for example. If there's a local company to do the work, there'll be even more in the bucket. That's why this handbook is called Plugging the Leaks.

There is a lot more on the concept of the leaky bucket in chapter 2, where we also explain why local economic development is a bit like irrigating a field – making use of all the available in-flowing money to increase local productivity. We have called it '*Plugging the Leaks*' to emphasise that stopping leaks is just as important as pouring new money in, or inward investment as it's sometimes called. We have added the strap-line '*making the most of every pound that enters your local economy*' to highlight that in-flows of money are our starting point for strong local economies.

So let's be clear: Plugging the Leaks is not about trying to close off a community from connections with the outside world. Instead it is about increasing local linkages in order to make maximum use out of all incoming inward investment, whether its source is government spending, business spending or consumer spending. This will make the community richer and so better able to buy from other communities those items or services that it desires that are not available locally. So we aren't arguing for self-sufficiency and isolation, ignoring very important inward investments. We don't believe in blindly adopting 'local purchasing programmes'. This sort of protectionism went out of fashion in the Dark Ages for a good reason – local businesses became complacent; prices rose and quality fell.

So while we think it is important to reinvigorate the local economy by fixing as many leaks as possible, we don't think the bucket is a universe unto itself.

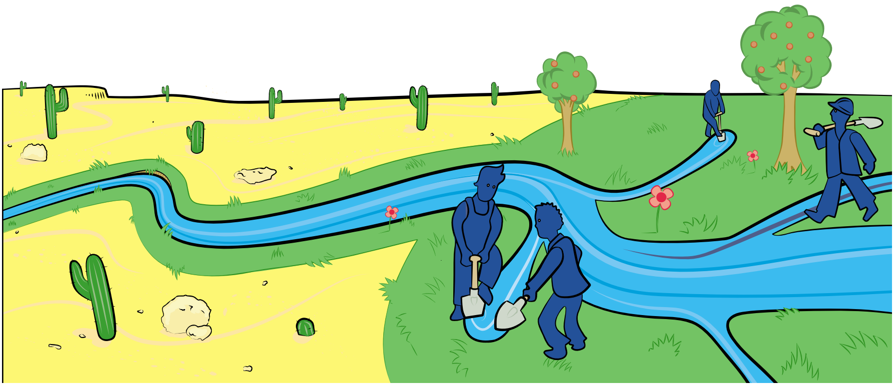
2: Understanding the local economy

In this chapter we develop the water-based metaphor for local economies that we introduced in chapter one. We start with how irrigation provides one way of seeing the local economy. We then return to the leaky bucket. We also slip in one or two concepts from economics that you may find helpful, as painlessly as possible.

Irrigation

Imagine some farmland in an area with not enough rain. You want to make that land more productive. So you construct a large irrigation channel to bring water in from outside. However you soon realise that this channel only makes the land fertile along its banks, it doesn't reach the whole area (like the left half of the picture below). So should you now build several other major channels to bring water in from outside? Not a bad long-term idea in case the main one dries up. However the most sensible first step would be to create mini-channels that can spread the water from the existing central irrigation channel so that more of the land can become fertile.

So it is with money flows. Inward investment is a large irrigation channel of cash into a poor area. This inflow could be welfare benefits, tourist income, or a new manufacturing plant setting up in your area. The inward investment is likely to directly help to employ people in your area. However it will only 'irrigate along its banks'; it won't employ everyone.



The community then has two ways to increase its productive capacity further: it can attract in additional inward investment; or it can create mini-channels off existing inward investment. These mini-channels are intended to enable money that is already in the community to be re-spent locally. This could mean businesses sourcing more of their staff or goods locally; or public authorities encouraging local firms to tender for contracts; or the community setting up a food co-operative or a wind energy production plant.

By exploring the major inflows of money into an area it is possible to identify opportunities for increasing the re-circulation of that money to other parts of the local economy.

A local spending policy

'Communities really benefit when enterprises invest their income back into the local economy – thinking in this way can truly prepare the ground for other small scale community enterprise.'

Sue Bennett of Eden Community Outdoors

Eden Community Outdoors (ECO) in Cumbria is very important to its local community – not only does it provide youth recreation facilities, it also has a 'Local Spending Policy'. In 2001, practically all of ECO's income (96%) was from sources outside Cumbria itself, yet ECO re-spent 60% of this income within a 10-mile radius of Appleby, thereby directly investing nearly £33,000 in the area as a result of their activities. An economic analysis showed that every £1 received by ECO led to £2.08 for that local economy. ECO realised that their local spend could have been higher if they had been able to use entirely local trainers. However in some areas of expertise they had to go outside to bring in new skills. They have now built up a skills base in the locality in which they work to help more of their money stay local.

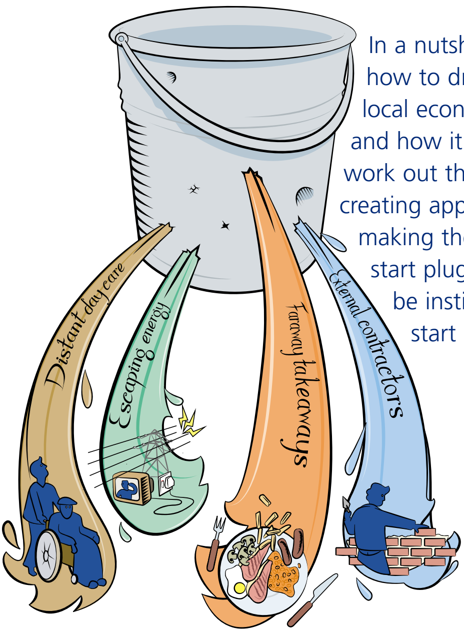
The leaky bucket

'There are so many holes in our local economy you could even say we didn't have a bucket at all!'

Bob from NEF's Boncath workshop

Imagine your economy as a bucket. The money that comes into your area will flow straight out again if there are many holes in the bucket. A full bucket means that local people have enough money to be able to buy what they need for a good quality of life. But if your bucket is leaky then to fill the bucket you will need to pour the money in at a faster rate than it is pouring out. So there are two strategies to fill a bucket – you can pour in the money faster, or you can slow down its leakage by plugging some of the leaks.

In economic terms that means you both focus on attracting more money into your area – inward investment, grants, welfare benefits, export sales and so on. And you slow down the rate of leakage through local sourcing, adding value locally, using local resources. We've become so obsessed with bringing in new money that this second strategy for economic development has recently been neglected. That's why it forms the focus of this handbook.



In a nutshell, the Plugging the Leaks workshop explains how to draw a picture of the leaky bucket for your own local economy – showing how money currently pours in and how it currently leaks out. The next step is to roughly work out the scale of the different leaks, the ease of creating appropriate plugs and how interested people are in making the plug. It is then relatively straightforward to start plugging some leaks. It is also an approach that can be instinctively understood by people so that they can start applying the logic to all aspects of their lives.