Regional and Business Studies (2015) Vol 7 No 1, 19-24
Kaposvár University, Faculty of Economic Science, Kaposvár

THE FEATURES OF LOCAL CURRENCIES AND THEIR SOCIAL BENEFITS

Károly SZÓKA
University of West Hungary, Faculty of Economics, H-9400 Sopron, Erzsébet u. 9.

ABSTRACT

Nowadays no one disputes the role and the significance of local currencies. We can find local currency and types of local currency initiatives in many places throughout the world. Local currency works similar to vouchers but is transferable and has secondary circulation. Local currency complements the trade in national currency andt does not seek to replace it. The role of a local currency is to connect economic and non-economic stakeholders, protect the local economy and also be used as an anti-crisis resource. Local currency systems have several advantages but during their configuration difficulties can occur. A local currency can only be operated through regional co-operation and for this the collaboration of the local governments, entrepreneurs and individuals is needed.
Keywords: local currency, benefits, difficulties, social aspect

INTRODUCTION

What is money? We can find a wide variety of definitions in economics literature and these are sometimes very different. That is why money does not have a real definition; we can define the role of the money by enumerating its functions. Meanwhile, money has changed into an infrastructural factor that allows the division of labour within the community, the flow of information and material among the participants of exchange activity and social agreements, and obviates acceptance, which is necessary to operate the institution of money (*Szalay*, 2008).

We can find local currencies and local currency initiatives in many places around the world. This type of initiative can be divided into two main groups. The first group is actually a self-help administration system that allows the members of a community to exchange goods and services among one another. These are known as community self-helping systems, exchange clubs, exchange and barter systems, favour banks or bee circles. The appellations and its contents are a bit different but the aim of each system is to link the missed opportunities to the unsatisfied needs of the community.

Some kind of simple system is used to register the exchange (e.g. Time dollars: "Time-keeper" software, Ithaca hours: „Ithaca Daily Journal" newspaper). The second group is the issuing of a local currency - a money substitute. There are those that hold their value (WIR, Kékfrank) but there are those that deteriorate in value over time (Chiemgauer, Urstromtaler).

Each system encourages the sale of local goods and services to operate in a particular location or region. They strengthen the regional economic ties and try to avoid negative economic effects, e.g. unemployment or the bankruptcy of firms or traders. Local currency defers from vouchers in several features. One of these differences is that while the economic circulation of vouchers is closed because they are only redeemable, a local currency is transferable, which is its most relevant function, and alongside this it creates a secondary market turnover. The other one is that vouchers have an expiration date; but local currency is a currency which normally has no expiration (*Madaras and Varga*, 2011).

KEY FEATURES OF LOCAL CURRENCIES AND MONEY SUBSTITUTES[1]

The role of local currencies is many-sided. The term "local" means regional cash equivalents and the term "national" means a normal official currency. On the one hand, local currency complements the deal with the national currency in a given region; on the other hand, a local money substitute links economic and non-economic actors. This currency cannot be used outside of the region, so the payment function is severely limited.

A local currency protects the local economy against harmful effects of external trade and by using one we can avoid the exclusive secondary multiplier driven development of the region's economy. If local income is received in local currency, then it will stay in the region, it will be spent locally. It also can be used as an anti-crisis tool. The amount of money in circulation is decreasing; liquidity, job opportunities, salaries and possibilities for taking different loans and credits are also decreasing, which is caused by the recent financial and economic crisis. Based on these factors, the members of the community suffer from a lack of money. The amount of issued "local currency" is deposited in bank notes or on different bank accounts, which ensures the safety of the procedure, although this does not actually mean money creation. Because of this, coverage shall be liquid. It cannot be invested – it is also different in each country – and this may be an obstacle to the organization's efficiency. In the start-up stage, it is really important to increase confidence, but later on it is possible to invest the deposits into appropriate investments, for example into liquid assets, such as government bonds. If someone buys these technical money-substitutes, he puts money into the institution which issued this "local currency," but the given institution has no right to have disposal of it because it is re-exchangeable with the national currency at any time. (Exemptions may occur, for example the WIR, which is not re-exchangeable.) Usually the re-exchange has a cost that can be classified between 2-5%. Banks do not provide credit in local currency; the only exception is the credit in WIR.

Another feature of local currency is that it works as a system with maturity and the owner must face the impairment of the currency, too. This means it will be devalued on a monthly or a quarterly basis, so it can lose its value, which is called demurrage. This demurrage provides – exactly accelerates – the usage of the local currency because it prefers consumption instead of savings.

---

[1] Based on *Tóth*, 2011

DIFFICULTIES AND RISKS

Of course, the system does not work by itself. For its sustainable operation it is absolutely necessary to set up an organization which considers the tasks of operation with a high priority. Such an organization has many tasks. One of the most important is to compile, manage and update a list about the participating enterprises; shops and markets where this local currency is accepted.

The proverb "Beginnings are scary" is especially true in this case since the launch of the system is not easy because at the beginning it is always difficult to convince enterprises to participate in this system. Persuasion, motivation and communication are also difficult. Powerful and innovative marketing- and public relations tools are required that will convince both businesses and potential consumers about the benefits of the system. Just think how difficult entrenched consumer habits are to change. One tool could be the so called "cheaper exchange," when a 5% discount is given. In these cases the redemption of 100 units of the national (local) currency is worth 105 units of the local (regional) currency. It is necessary to involve people with relation (ship) capital and also the media, whose opinion is significant due to the exposure accorded to statements they make. Therefore, the local media have a community forming force. It is not enough to stand behind the issue once, but it is a must to continually involve the participants and supporters into the publicity. The citizens may mention on the negative side that they are running into a loss with this system because, contrary to the standard bank deposits, they are not receiving any interest. The lack of state-backed guarantee and the possibility of forgery are also risks in building confidence in a local currency, since it is simply made of paper and cannot have as many safety features as a national currency. Issuers of local currency take this issue into consideration, of course. Based on their opportunities they emit this currency in the best possible quality, with safety features that are usually developed in cooperation with the banknote printing company of the given country[2].

Of course, the circumstances and the regulatory conditions are different from country to country, but this is caused by the absence of a precise regulatory background. This is the situation in Hungary, too.

Precise regulation is missing concerning (Based on *Helmeczi and Kóczán*, 2011):

- the redemption of vouchers to legal currency and redemption commission,
- the awareness of the potential changes with the stakeholders,
- prohibition of the emitted unsecured vouchers, potential bankruptcy by a financial institution,
- the way to deal with the coverage, to protect the coverage in case of liquidation
- restricting other activities by the voucher emitting companies,
- the allocation method of the profit from coverage and commission.

2 Due Tamás Perkovátz it would be the greatest success of the Sopron Blue Frank, if forging it.

The formal requirements must be regulated (*Kovács et al.*, 2011):

- printed voucher or electronic currency,
- what should be the name of the surrogates,
- exact determination of the amount and denominations of the voucher emitted,
- what should be the source of the costs of the planning, positioning and preparation of safety features, and
- should there be any cost for exchanging to the official currency (and if so, how much should it be).

It also poses difficulties if the local currency does not play its role, it does not remain in circulation long enough. It (this circulation period) basically depends on whether the supply of goods and services that are available in the local currency (voucher) are attractive enough or not. We must also examine whether the sellers (enterprises) who sell in the local currency can find a source of supply for their product or services where they can pay with local currency too, because their aim is not the accumulation of local currency.

THE SOCIAL ASPECTS

The first thing that must be mentioned is "Community Togetherness," or rather the lack of it, and its strengthening. Since the local currency connects economic and non-economic actors, it increases the feeling of togetherness by communicating that it is our common interest to trade with each other. The income generated should remain local and the participants should enrich each other.

The demurrage, which is the declared expiration date, is a tool for this. The expiration and periodical devaluation makes the region and people physically interested in using the "local currency". If people take this opportunity, then the "local currency" may circulate even faster than the national currency. If the same note of the "local money" circulates several times before its expiration date, it may generate more revenue and income for the enterprises and organizations. Since people/enterprises will trade with each other in the region it will strengthen and increase the cooperation among the already cooperating parties.

The issue of seigniorage has to be mentioned also. While issuing national currency we are talking about real seigniorage: revenue money creation by the central bank generates a special kind of revenue which flows indirectly to the state budget. Local currency is covered by the collected deposit money. A given part of the coverage must be permanently available. The free reserves are investable, its profit called the gross "seigniorage" income. As I already mentioned, the operating of the system has costs (e.g. designing, printing, defence against forgery, marketing, etc.). By subtracting these costs, we receive the net seigniorage, which is the gross seigniorage reduced by the operating costs (*Madaras and Varga*, 2011). Using local currency as a surrogate will reduce payments done by cash. This procedure will decrease the income of the central bank and at the same time it will decrease the state budget too. The users of "local currency" consider the evolving social benefits in the region more beneficial than this seigniorage loss (*Kun*, 2006). Since the amount and turnover of local currencies is negligible compared to volume of national currencies all over the world, central banks do not block the introduction and use of local currencies. The topic of retention and expansion of job opportunities is very important nowadays.

It should be investigated whether salaries should be paid in local currency in the region or not. If only a part of the salaries are paid in local currency, this mentioned amount will be spent in the region, therefore, that part entirely remains in the region. It is also likely that people who are receiving their salaries in a local currency will not entirely exchange it to the national currency. Probably they will spend it in the region and this indirectly – almost immediately – may create jobs; but at least it saves them. Of course it is a must to have those goods and services available which are needed for the customers[3].

For a practical reason it is also recommended that the local currency would not be printed but it would be "issued" in an electronic way that would end up with a more appropriate usage in today's age (some kind of card-based solution). The "PayPass" solutions which are really popular and spreading nowadays are also a possibility for low-amount payments. The local governments have – or might have – an extremely important role. A local currency can be really successful if it is not working as "a private initiative" only, but the local government takes an active part in it too. An important issue is the wages and the payment of common charge. It is suggestible for the local government to give a part of the wages in local currency – the first concerned parties could be the public servants or the civil servants at least. The spread of local currency could be helped by the so called "cheaper exchange" solution, which means that the local government pays wages at a higher percentage in the local currency than would be paid in national currency.

After implementing the above mentioned provisions (paying the salaries in local currency), the payment of different aids and subventions should be the next step. It would contribute to the system's efficiency if common charges (such as local taxes, overheads) would be payable in local currency. In that way the local businesses that are participants in the system and receive their income in local currency will be not interested in exchanging their "vouchers"/local currency. Local government has many costs that can be paid in local currency to those acquiring local enterprises. Personally, I cannot imagine the sustainable development of the system without the active participation of municipalities.

CONCLUSIONS

The introduction of local currencies is not a new way of thinking, however here in Hungary it only recently came into the spot light. Several arguments can be listed to strengthen the proposition of introducing and using local currency as a protection/defense of local economy, for the creation of workplaces, and cohesion of the local community. By introducing a local currency, a part of the local

3 A good example is the Balaton Lake Korona that can be spent preferentially at the shops of Pólus-Coop Ltd.

consumption could be retained locally. The local acquiring enterprises could be the basis of the system, because they will spend the received amount in the region, which will promote the growth of the local economy. There are several questions arising in relation to this system, such as the regulation background, safety, human background, and the mechanism of real usage, marketing, and the attitude of the local government. There is no clear line between the weaknesses and strengths; economic development is our common interest. The problems should be solved, the advantages should be used. If this will succeed and the local community will become a partner in this procedure, it may benefit the rise of the local economy. I would like to finish my study with a phrase commonly used in the medical sector: "Use it to be useful!"

REFERENCES

Helmeczi, I.N., Kóczán, G (2011): About the vouchers called local currency (in Hung.). In: MNB szemle, 2011. Április 40-41. p.

Kun, J (2006): About the surrogates (in Hung.). PSZÁF tanulmány, [online] <URL: http://issuu.com/helyipenz/docs/namedd5164 >

Kovács, T., Légler, N., Vágyi, F.R. (2011): The relation between the local currency and the local government (in Hung.). In: Adóz(z)unk a jövőnek? Professional conference on finance, taxation and accounting, Sopron. 6-7. p. [CD-ROM]

Madaras, A., Varga, J. (2011): The seniorage effect of the local currency (in Hung.). In: Lázár, E. (Ed.) Gazdasági és üzleti kihívások a Kárpát-medencében. Csíkszereda: Státus Kiadó, 225. and 228. p.

Szalay, Zs. (2008): The revolution of the tame money (The creation of common property-based monetary system) (in Hung.). Budapesti Corvinus Egyetem 93. számú műhelytanulmány, Budapest. 2. p. [online] <URL: http://edok.lib.uni-corvinus.hu/284/1/Szalay93.pdf >

Tóth, B. (2011): The role of local currencies in the development of local economy (in Hung.). In: Pénzügyi Szemle. 56. 1. 67-68. p.

Corresponding author:

Károly SZÓKA
University of West Hungary
Faculty of Economics
H-9400 Sopron, Erzsébet u. 9.
Tel./Fax: +36 99 518-257
e-mail: kszoka@ktk.nyme.hu