

Economy of Second Life

The virtual world *Second Life* has its own **economy** and a currency referred to as **Linden Dollars** (L\$). In the SL economy, users (called “residents”) buy from and sell to one another directly, using the *Linden*, which is exchangeable for US dollars or other currencies on market-based currency exchanges. This economy is independent of the price of the game, which users pay to Linden Lab, not to each other. Linden Lab reports that the *Second Life* economy generated US\$3,596,674 in economic activity during the month of September 2005,^[1] and as of September 2006 *Second Life* was reported to have a GDP of \$64 Million.^[2]

In 2009, the total size of the *Second Life* economy grew 65% to US\$567 million, about 25% of the entire U.S. **virtual goods** market. Gross Resident Earnings are \$55 million US Dollars in 2009 – 11% growth over 2008.^[3]

1 Basis

The basis of this economy is that **residents** (that is, *users*, as opposed to Linden Lab) can buy and sell services and virtual goods to one another in a **free market**. Services include **camping**, working in stores, custom content creation, and other personal services. Virtual goods include buildings, vehicles, devices of all kinds, animations, clothing, skin, hair, jewelry, flora and fauna, works of art, and breedable in-game animals and pets such as: foxes, turtles, horses, cats, dogs, fish, dragons, and original in-game pets called Meeroos. To make money in Second Life, one must find customers who are willing to pay for the services or products that one can supply, just like in real life.

Because of the existence of *virtual land*, there is an active **virtual real estate** market. Originally all land comes from Linden Lab (which is part of the pricing and a revenue stream for them), but after that it is bought and sold much like real-life real estate. Mainstream media has reported on SL residents who earn large incomes from the SL real estate market.^[4]

In addition to the main economy, some residents receive a small weekly stipend, depending on the kind of account they have, and when they joined Second Life.^[5] There are also the virtual equivalent of minimum wage jobs and charitable organizations that try to introduce new residents to the consumer economy.

Another option for making money in Second Life is “camping”. Throughout the virtual world are locations

where SL members can earn money by either sitting, doing an activity such as dancing or painting, or another similar activity; payment is offered consisting of so-many Lindens for time spent. The money is paid by scripted objects owned by the land owner, usually to increase the search ranking of their store or other venue, and many forms of camping are officially forbidden by Linden Lab, though enforcement of this rule is sporadic. The amount of Lindens paid and the time interval varies from place to place, and some landowners pay in virtual goods rather than Linden Dollars. Since this could result in some users leaving their avatars “camping” for days at a time, accumulating thousands of Lindens, most locations forbid 24/7 “camping” and some camp options limit the amount of money that can be made in a location over a period of time. As of January, 2010, Linden Labs has prohibited camping for lands which are enabled for “search” because traffic is one of the important criteria for search rankings.

2 LindeX currency exchange

Residents may purchase L\$ directly through the client, or convert between Linden currency and U.S. currency through either Linden Lab’s currency brokerage, the **LindeX Currency Exchange**, or, in the past, other third-party currency exchanges. As of August 1, 2015, the Authorized L\$ Reseller pilot program has been closed, and the LindeX is the only authorized place to purchase L\$.^[6]

The ratio of USD to L\$ rarely fluctuates as Residents set the buy and sell price of L\$ offered on the exchange. Between February 2008 and February 2011 the rate has remained stable with a high of 270 and a low of 240 per USD.^[7]

3 Economic issues

3.1 Government

Second Life residents mostly do not have a government. In part this is enabled by the fact that there is also no physical damage, and in principle no possible theft of property (excluding virtual content), nor is there war on a large scale, other than between military groups or other role players restricted to “damage-enabled” sims like Eridanus and other similar areas. Thus, many of the functions of government are not required.

On the other hand, there is always a need for dispute resolution.

At the lowest level, property rights reign supreme. A building's owner makes the rules, and can simply eject or ban any resident he or she wishes to, with or without cause. An owner of 512 square meters is lord of that manor, just as the so-called **Land Barons** are the lords of their much larger ones.

Some groups of people in Second Life have created small-scale political structures. For example, they might band together, purchase property in the group's name, and agree to follow in-group rules and regulations, elect officers, support a monarchy, etc.

At the highest level, Linden Lab is the true owner of Second Life, and within the **Second Life Terms of Service** (TOS), they are the ultimate authority.

3.2 Legal position of the Linden Dollar

Linden Lab has been marketing SL as a viable business channel for making real money, while at the same time including provisions in the Terms of Service which give Linden dollars no intrinsic value as a form of currency.^[8] Linden Lab is not required to pay any compensation if L\$ is lost from the database.^[9]

3.3 Monetary policy

In addition, recent articles^{[10][11]} published by the **Ludwig von Mises Institute** warned that while Linden Lab maintains a **currency peg** of about L\$270=US\$1, it is only partially backed by Linden Lab's revenue in US Dollar, as there is a perpetual deficit between Linden Dollar creation (from stipends, see below) and **USD** revenue received by Linden Labs. The difference is made up by Linden Labs creating Linden Dollars out of nothing (just as governments turn to the printing press to **create money**). This might lead to a recession if Linden Labs is forced to tighten its monetary policy, or an outright economic collapse if people lose confidence in the peg's sustainability (see **hyperinflation**).

In light of this, Linden Lab has been gradually lowering the amount of the Linden Dollar stipend paid out to residents. In the past, basic accounts received L\$250 starting money plus a L\$50 stipend every week that they logged in. The weekly stipend was ended for accounts created after May 29, 2006.

In similar fashion, the Premium stipend has fallen from L\$500 to L\$300 over time, though for each individual the stipend in effect at sign-up time remains in effect.

Currently, Lindex exchange rates run L\$240 per US\$1 on average, with variations of about 5% at various times. On SLX exchange, and other independent exchanges like ACE and BNTF, rates run higher, L\$275–285 per US\$1,

possibly because Linden Labs process credit system takes 5 days to deliver the withdrawn funds, while independent exchanges pay out much quicker, indicating a premium for prompt delivery.

3.4 Acts of Linden

Linden Lab, as the actual owner of all the software and server-side hardware that makes up Second Life, has the ultimate authority to change all aspects of the world, from the economy to the physics to the terms-of-service.

Changes made or proposed by Linden Lab are thus far-reaching and can lead to unexpected results. Some changes have had the effect of creating new markets, but also have on occasion destroyed or removed the value of existing ones, or inadvertently given a market leader at a particular time unique advantages that entrench them as a market leader in the future. Some say that unless this power is very tightly controlled and transparent, the Linden economy is unlikely to attract very large investment.

One example is *InfoNet*, an in-world newspaper and information delivery service run on a for-profit basis, and formerly of limited effectiveness due to a limited range of access points (true of many such systems in SL). When the old concept of "telehubs" was removed from the game, Linden Lab replaced them with "InfoHubs", each of which included an InfoNet access point which was hosted for free on system-owned land; it also placed InfoNet access points in the Welcome Areas where new users arrive, where no user is normally permitted to leave business-related objects. This had the effect of giving InfoNet an instant and substantial advantage.^[12]

Recent Linden Acts of greater economic import include the **banning of wagering** on games of random chance or on real-life sporting events with L\$. As soon as the rule change was announced, casinos were given a few days to close. Casino owners and game makers either found other avenues of business or ceased trading. The fallout of this was the largest bank in SL, **Ginko Financial**, which had its ATMs in most major casinos, saw its reserves drained completely within hours, and was never able to catch up with withdrawal requests, which eventually amounted to L\$55 million out of deposits of L\$180 million. Ginko's assets were primarily invested in things of either poor to no **liquidity**, or virtual securities that were then trading at significantly under their purchase price. Ginko was forced into insolvency and converted their depositors into bond holders on the **World Stock Exchange** (one of several in-world stock exchanges).

Shortly after these events, Linden Lab began collecting the **Value Added Tax** (VAT) from customers who live in the **European Union** (aside from those customers who have a **VAT ID** which exempts them from the tax). This is applied to membership, land purchase, and land maintenance fees paid in real world currency (e.g., the **euro**) by European members to Linden Lab. Previously, Linden

Lab had absorbed the cost of the VAT.^[13] Linden Lab did attempt to collect any VAT which might theoretically be applicable to Linden \$ transactions between individual Second Life residents. When VAT charging on fees began, there was discussion among Europeans about leaving SL, or else transferring their lands to American partners, or getting into lines of work that do not involve fees paid to Linden Lab in euros. American Land Barons were in a position to offer tax shelters to Europeans (although in theory the European users could still owe VAT on cash transfers to or from their US partners.)

3.5 Linden Economy Factors

Because some business models rely on a revenue model existing outside Second Life, some businesses may affect the traditional approach to Second Life business and the general Second Life economy. For example, the *SLIPP-cat* advertising system encourages companies to provide content in Second Life which can not only be obtained for free but which *generates income* for its owner by displaying advertisements to other users when clicked.

SL businesses are especially vulnerable to *business disruption* due to the zero^[14] marginal cost of production. In 2007, *Anshe Chung* was criticised for marketing a line of furniture in which every item was sold for 10 Linden dollars (approximately 4 cents.)^[15] Selling such items was viable for Anshe because the majority of her income came from the sale and maintenance of land, used to host houses within which the furniture was placed; but posed a threat to furniture makers as such low prices would make it impossible for stores not supported by an auxiliary business to compete.

In November 2009, Linden Lab announced that it was considering charging a L\$99/month per-item fee for listing “freebies” (free items) on XStreetSL, its *e-commerce* website, which previously could be exchanged for free on the site. It also announced XStreetSL would charge higher commissions for non-freebies, along with an L\$10/month per-item fee for such items. This was seen by the user community as a ploy to minimize the number of free and low-priced items on the site.^[16]

The low cost of business in SL allows unprofitable business models to be sustained at a lower real world cost than would be possible for the same business *in real life*.^[17]

4 References

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5 External links

- Investing in the online property boom

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6.1 Text

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