

The Global Economic Downturn, Philanthropy and Nonprofits:

Reflections on what it means, and what to do

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Introduction

That the global financial crisis is already impacting philanthropy and nonprofits is clear to everyone who follows daily reports of cancellations of charity drives, closings of programs, and even bankruptcies, or learns about economic troubles at one philanthropic institutions or another. It is also clear that the crisis' impact is going to spread and deepen for some time to come. Less clear is for how long the crisis and its fallout will last; and especially unclear is what the crisis ultimately means for nonprofit and philanthropic policy-makers, leaders and managers. How could they respond to growing uncertainty in the sector itself as well as in the various fields in which nonprofits and philanthropies operate?

At one level, little can be done. The current economic downturn, triggered by the financial crisis, is closely related to the inability of governments and international institutions to address what experts call the global governance problem -- the growing mismatch between the forces of globalization (largely financial), and the capacity of governments to steer and regulate. Illustrative of this problem is not only the financial crisis itself but so are the often hapless responses in political capitals around the world: no national government, including the US, China or Japan, and no international institution, including the World Bank, the IMF or the European Union, are able to deal with the scale and scope of current weaknesses in the global economy. So unless the systemic failures of governance are fixed through policies and institutions more adequate to the challenges of a globalized economy and global financial markets, much remains political impression management at worst and 'doctoring with the syndrome' at best.

At another level much more can be done, not in the sense of the global or macro issues mentioned above, but in terms of pro-active policy initiatives and management responses for, and on behalf of, philanthropy and nonprofits. This level, and what it means for operating nonprofits and for grant-making foundations, is the primary focus of these *Reflections*.

But before delving into concrete issues, options, and courses of action, two preliminaries are worth stating. First, why the current crisis occurred (because it originated in financial markets beyond the control of policymakers and leaders in the field) is of less interest than how to deal with its fallout in the short term, and how to develop strategies for the medium to long term. This is the case for operating nonprofits generally, and entails a very special call for foundations, in particular those holding large portfolios in stocks and bonds. Second, it is equally important to separate what would have happened anyway and what has happened additionally, sooner, or more forcefully because of the crisis.

What would have happened anyway...

Of course, while we can never know alternative futures, we can nonetheless reasonably extrapolate from developments that have taken place over the last 10 or so years, and identify a number of patterns and trends. Among these are:

- Greater demand for nonprofit goods and services combined with less, and more competitive, public funding
- Competition models developed elsewhere (health, social services, education) being applied to many other fields where nonprofits operate, with an emphasis on cost control rather than outcome quality
- Search for new business models for nonprofits in many fields, from health to arts and culture and from higher education to social services, to compensate for lower levels of government support
- Professionalization of finance, management and service delivery, often combined with a certain tameness even timidity in terms of advocacy
- Policy emphasis on greater civic engagement and fiscal transparency for legitimacy reasons
- Fluctuating private philanthropic support, as this source of funds is, and for good reasons, often fickle, and overly optimistic expectations about what foundations can and should do (e.g., substitute for reduced government spending).

What these developments would have meant is more than a rhetorical question, and for the simple reasons that these very trends are continuing, albeit in the context of a profound crisis. For one, substitutability processes between nonprofits and businesses would have become more frequent in regulated quasi markets (health, social services), as would have conversions of public to private institution particularly (education, culture). In other words, many organizations would have changed form, many nonprofits would have become more like businesses, many public institutions more private, and public-private partnerships more frequent and more complex.

In turn, this would have brought about fierce and long drawn-out debates: about the right revenue structure for nonprofits and the optimal mix of earned income, public funds and private donations, including foundation grants; about asset management and acquisition policies; about barriers of exit and (re)entry for donors and recipients alike; about stakeholder involvement (consumer, client, member, funder, staff, the general public etc); and, professional control over mission and operations, and the role of the board; about social entrepreneurship and nonprofit management and leadership styles; and, very prominently, about the role of foundations.

What is new now...

What the economic crisis adds now is a potent mix of new challenges to what was an already complex set of issues:

- At the societal level, there is a loss of trust in the 'system', a general sense of insecurity among populations, and opportunism both among some political actors, on the left and on the right;
- European governments, many fiscally sounder than the United States and with more room to maneuver, rediscover Keynesianism and interpret it to their own political advantage that typically result in some massive public spending program or another (of which only a rather small portion is likely to reach nonprofits). Increases in public investments are combined with reductions in current budgets, and create shortfalls, of which some, often indirectly, are passed on to nonprofits.
- Businesses engage in short-termism in trying to calm shareholders; they are cutting corporate social responsibility and giving programmes, including funding aimed at nonprofits; they are looking for government handouts and subsidies in return for some guarantees, typically employment and performance related.

- Philanthropic foundations have seen drops in asset values of scales not seen in decades, and continue to expect more losses, especially in the book value of stocks; they anticipate reductions in grant payouts, amidst concerns about the sustainability of current programmes and commitments, and put growing emphasis on asset protection.
- Many households have been and are facing both greater financial uncertainty and declining net worth, which could lead to drops in donations, even a break up of donor pools, and a decline in volunteering.

For nonprofits, the current crisis means fewer resources in terms of current expenditures for ongoing and planned programs; however, depending on public spending priorities, it may also yield some additional funding for investment programmes; but first and foremost, it means greater financial instability, more uncertainty for management and staff, possibilities of unfulfilled contracts and obligations, and unmet demand. For foundations and philanthropies generally, the crisis means balancing increased demand for support on the one hand with reduced assets and current as well as projected grant disbursements on the other.

What to do?

The reaction of boards and management could easily fall victim to common extremes in how organizations under threat react to unknown levels of uncertainty: on the one hand, to a 'do nothing approach,' either because of denial or fatalism; and on the other, to different forms of over-reaction and blind activism. Both extremes lead to high failure rates. There are, however, other options that reveal themselves only when appreciating what sets nonprofits and philanthropic institutions apart from other forms. Three characteristics are central:

- The presence of deeply embedded values (religious, political, humanitarian, moral, artistic) is a distinct feature of many nonprofits and foundations. How far they influence organizational behavior varies, but the significant presence of values implies at the very least a more complex means-goal relationship between operational and ultimate objectives. These values can be enabling or restraining; protecting or stifling; leading or misleading; invigorating or distracting.
- The presence of multiple stakeholders (trustees, staff, volunteers, users / clients, state agencies, grantees etc) makes nonprofits and foundations

inherently political organizations, and turns managing them into a complex task of creating and coordinating coalitions around a common purpose.

- The presence of multiple revenue sources (market, quasi-markets, membership, various forms of transfers from government, various forms of donations and sponsorship, contracts, etc) sets nonprofits apart from both business firms and government agencies; while foundations do not have multiple revenue streams, as primarily endowment-supported organizations, they require nonetheless significant public legitimacy and political/cultural capital to justify the tax privileges granted and the far-reaching autonomy allotted.

Thus, foundations and nonprofits are value-based, multi-stakeholder and multi-support organizations. By implication, if they are not rooted in values, if they have a dominant or single stakeholder, and if they are single-support organizations, the more similar they become to either market forms or public agencies.

What is more, price mechanisms, the best indicators of performance, are frequently absent in areas and fields where nonprofits and foundations are operating. This means that nonprofit and philanthropic leaders manage value-based organizations with multiple support streams under performance uncertainty -- a challenging task in the best of times. But does this mean in the current crisis? What can be done? Quite a lot, it turns out. Here are short term options for nonprofits:

- Begin with values and mission, and revisit the value base of the organization. If values are the foundation of the organization's mission, reinvigorate their meaning and make them relevant by basing all major decisions on values rather than economic rationality alone; if values are less central, make economic sustainability a priority.
- Consolidate resources around programs that are mission critical and resource attractive; conversely, prune activities that are less mission-critical and less resource attractive. Align stakeholders accordingly and build appropriate coalitions, and invest and divest accordingly.
- Cooperate only around mission central programmes, and consider merger and franchise models.
- Cross subsidize only if less mission critical programmes have a proven and significant capacity to generate revenue. Rededicate assets and reserves accordingly, and divest other cross subsidizing programmes.

- Spread risk in revenue and support streams by avoiding dependencies on government, donors etc., and by diversifying earned income options (sliding fees, charging above marginal costs, using assets, cross subsidizing etc).
- Run an active information campaign about what your plans are and how you seek to achieve them. Transparency and public awareness across stakeholders is important for any short term reorganizations to find legitimacy and success.

These options all start with the same hard question: What is more important, our values or the organization created for them? For many, the result will be a smaller and leaner nonprofit, one shaped by short term reactions to a crisis to sustain operations. It may not yet be a nonprofit forged as a strategic response to a changed environment, and with long term sustainability in mind. Therefore, nonprofits can engage in strategic planning and visioning by asking tough questions about their very existence, functioning and impact. Options include:

- Specialization versus generalization of programmes, target groups, fields etc
- Considering achieving a scale of operations adequate to both mission and resources
- Building partnerships and networks along economies of scope
- Exploring multisite and franchise models for scale economies
- Engaging members and users more by activating value commitments to reduce costs and create buy-in
- Reinvigorate lobbying and advocacy; be heard and voice concerns, and demand government funding when appropriate.

Many other options are feasible as well. The main point is that nonprofits have to be pro-active and inventive in responding in the medium term to the fallout of the current crises. Yet what can be done to prepare for future one? Such measures include:

- Exploring institutional innovations for the nonprofit field as a whole: e.g., dedicated financial institutions for nonprofits including insurance funds, forms of capital markets for social investment etc, including smart public private partnerships with profit-making functions and reserve options.
- Establishing a Public Trust Fund for nonprofits to smooth eligible organizations over fiscal uncertainties, budget shortfalls etc. Of course, there are different ways of how such a trust fund could be built (tax-based, community foundation model) and run.

- Developing membership bases that can be mobilized politically for advocacy purposes and economically for resource generation.
- Seeking nonprofit liaison or focal points in key government areas for philanthropy and nonprofits, and create 'philanthropic listening posts' as early warning system nationally and internationally.
- Investing in more and more effective nonprofit advocacy, and strengthened the watch-dog function of nonprofits.

What could foundations do in the medium to long term? To some extent, their options and actions are addressed somewhat implicitly in the above recommendations. Like nonprofits, they need to ask hard questions that go beyond asset protection and servicing current obligations. Unlike nonprofits, which have to deal with many pressing questions around their very own sustainability, foundations face a different set of challenges. These are less obvious and linked to their special role in today's society.

Foundations have significant comparative advantages over other institutions. The signature characteristic of the modern foundation, its independence both from market considerations and election politics, means that it is among the most autonomous institutions of modern societies. They can take the long term view, and are less beholden to short-term economic and political expectations. As a result, foundations might well be better positioned than other institutions to contribute to society in four distinct ways: they can be

- **Social Entrepreneurs**, identifying and responding to needs or problems that for whatever reason are beyond the reach or interest of market firms, government agencies, and existing nonprofits. Foundations can strategically intervene and provide support that would otherwise not be available at the right time, in the amount needed, and with conditions tailored to the need.
- **Institution Builders**, identifying coalitions of individuals and organizations capable of implementing a program or course of action across sectors, regions, and borders; mediating conflicts, convening, and in general assuming the role of 'honest broker' among parties; offering financial resources as well as knowledge and insights to help new entities become self-sustaining.
- **Risk-Absorbers**, investing where there is great uncertainty that an investment will yield a return and that actions will bring about intended benefits; foundations can be especially well-placed to invest in untried initiatives

(medical, educational, social . . .), in basic research, scholarship, writing, and artistic production, and in politically sensitive and unpopular causes.

- **Value-Conservers**, supporting practices, virtues and cultural patterns that cannot easily be supported via markets or win funding from governments that must answer to bare majorities.

Financial means are only one of the resources employed by foundations in playing out these advantages. Knowledge, legitimacy and autonomy are others. These qualities and resources of foundations are well suited to help nonprofits and the constituencies and interests they serve to deal with are central element of the current crisis and the global governance problem that is at the core of it. That element is risk, and the contribution foundations can make is best summarized by what could be called the pro-active precautionary principle. To appreciate the import of both, it is useful to take a closer look and to keep in mind that the current crisis is linked to globalization.

Climate change, the 2008 financial meltdown, the 2009 economic downturn, terrorist threats or fluctuating food or oil prices have in common that they involve unknown risks and latent risk communities that can neither easily be calculated nor managed. However, the calculation and management of risk was part of the 'master narrative' of modernity: the state was designed to protect and insure citizens against risk - the dangers posed by nature, personal risks of ill health and unemployment, as well as threats posed by foreign enemies. That concept of risk assumed its most developed expression in what has become known as the precautionary principle of policy-making. It states that threats of serious or irreversible damage *and* lack of full understanding are no reason for abandoning or postponing preventive measures. The principle originated in environmental planning and has expanded to other fields such as the chemical industry, climate change, and even the threat of terrorism.

However, whereas the principle sought to establish an explicit link between cause and effect, the risks of today's globalized world are of a qualitative different nature. Risks cross borders, often in unpredictable ways; they may be far into the future, and with uncertain timelines; and they are increasingly the cumulative outcome of the actions of many individuals and organisations. Sometimes, these risk communities are latent and defined by the possibility of some highly unlikely event, such as the citizens of Iceland, the bank managers of Lehman Brothers, home owners in California's Inland Empire, laborers in Shanghai, and house servants in Dubai. Risk communities, framed largely in national and regional policy contexts, are becoming

increasingly linked, in ways that are frequently unknown and ill-understood. In other words, risk communities and the global governance problem are closely linked. Risks have become unbound.

What institution can help rebound risks in a globalized world? Foundations, endowed with their four comparative advantages, can step forward and help face this challenge. They can make sure that risks are better understood and attributable in terms of benefits and costs, even across boundaries, time and social class; that the regulatory framework for policy action have capacity regulating in the first place, and with effective enforcement mechanisms ready for action. Foundations can create arenas where risks are enunciated, exaggerated, discounted, debunked, assessed and debated. They can build arenas that encompass information, expert knowledge and reasoned deduction as well as fears and prejudice, but above they can help provide forums for expressing and communicating differential knowledge about risk, be it in the field of finance, health care, the environment, communication or housing.

Thanks to the financial crisis of 2008, broad ranges of fields and institutions suffer from a lack of trust and increased uncertainty. They are riddled with externalities and ripe with opportunism; yet at the same time, the fields and institutions present many opportunities for creating public benefit. Here, in this quintessential 'problematique' of a globalized world, foundations could find a strong calling and purpose. Foundations could help identify latent communities of risk (and benefit!), and encourage adequate monitoring and enforcement mechanisms in fields where national and international governments, due to the global governance problem, cannot implement the precautionary principle. In other words, the financial crisis has opened up a new *raison d'être*, a new role for foundations: identifying, managing risk and building appropriate institutions and coalitions for and among risk communities – in other words help rebuild institutional trust, not in a narrow economic sense but much broader in terms of a social and cultural confidence that globalization world for and not against people.

Conclusion

Sociologists and economists have long argued that crises are the necessary correctives of capitalism, part of an ongoing process of the 'creative destruction' that has shaped much of the modern world, with globalization as the latest, current development. If this is the case, the crisis offers perhaps as much in terms of

opportunities as it contains challenges. It will lead to the demise of some nonprofits and the rise of others, some will flourish and others become less relevant, moribund, and defunct and may even disappear altogether. Some foundations will rise to become icons of 21st century philanthropy; others will struggle to meet increased demand for grant support and become defensive and reluctant donor institutions. Leadership and elites in nonprofits and philanthropy will be replaced, at least partially. New funding patterns, business models and ways of organizing are likely to emerge.

Responding to a crisis then means both: reducing uncertainties and capitalizing on opportunities. Yet above all, mastering the crisis requires a pro-active stance on behalf of philanthropic and nonprofit leadership – not by asking for old wine to be served in new bottles (as the American car giants or many have been doing), but by embracing what philanthropy stands for: making space for creativity and innovation and preserving past achievements for the benefit of all.