

# Downstream and In Demand

Another Look at Mid-South Nonprofits and the Economic Crisis



A report from the  
Alliance for Nonprofit Excellence  
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# Executive Summary

The more than 3,000 organizations that comprise the Mid-South nonprofit sector are a vital part of the region's economy, identity, and quality of life. The Memphis area is known for its treasures—cutting-edge medical facilities, unmatched musical talent and heritage—and for its hardships—poverty, crime, struggling schools, chronic disease. For decades local nonprofits have worked to advance the former and alleviate the latter, preserve and promote our assets and solve our worst problems. They have traditionally done so with meager resources, stewarding their limited funds to fulfill their mission and meet overwhelming needs.

The recession that began in December 2007 has had severe and lasting effects on local nonprofits already stretched by funding gaps and unmet demands. All major nonprofit funding streams dropped off, including foundations, corporations, government agencies, and individual donors. Grants and donations plummeted along with world financial markets, leaving nonprofits scrambling to cut already emaciated budgets. At the same time, a poor economy means increased needs—unemployment, foreclosures, and the loss of health care and homes rapidly increased the number of people relying on nonprofit programs and services.

In the summer of 2009 the Alliance published *Downstream and in Demand*, a study of the impact of the recession on the local nonprofit sector. The report was the first to compile a comprehensive look at the extent of the financial impact on local organizations, as well as the strategies emerging to survive the crisis and the most important areas of risk and need. In the spring of 2010, we began another study to determine what had changed over the last year and to update this snapshot of the sector as it struggles with continued revenue losses and growing demands.

*Downstream and in Demand II* is an analysis of data collected from 146 leaders through a 40 question survey and focus groups conducted with sixteen leaders during June 2010. Participants represent more than 30 fields of work, with the largest numbers of respondents in arts and culture, children and youth, health, education, and human/social services. Organizations ranged from those with no employees to those with more than 500 employees, with more than half having less than 25 employees. Half of the respondents have budgets below one million dollars, 28 percent are in the mid-sized range of one to five million, and 23 percent have budgets over five million dollars.

## Key Findings

### Financial Impact

- Thirty-five percent of respondents experienced revenue declines in the last year, with another 29 percent maintaining their revenues at last year's level. Forty percent of small organizations experienced declines, and a quarter of both small- and mid-sized organizations experienced declines of more than 20 percent of total revenues. Thirty-seven percent of respondents saw increases in revenues.
- Last year 73 percent of respondents reported revenue declines. Even though many nonprofits

appear to be experiencing decreasing rates of decline, many are still below pre-recession levels.

- Twenty-nine percent of respondents will end the current fiscal year with an operating deficit.
- Fourteen percent of respondents have no cash reserves and 34 percent have one to three months of reserves. The number of respondents that have more than a year of cash reserves increased this year from one to thirteen percent.
- Forty-eight percent of respondents reported applying for a line of credit in order to stabilize their finances and only 48 percent of these successfully obtained credit. Sixty percent of large organizations that applied for credit were successful, compared to only 37 percent of small organizations. The tightening of the credit market has made banks less willing to engage in small transactions, and made it more difficult for organizations with fewer assets to access credit lines.
- Because of the labor-intensive nature of their work, a necessary lack of economies of scale, and the inelasticity of prices (e.g., neither low-income uninsured people nor third-party payers will cover the full cost of services), nonprofits must frequently subsidize their programs and services with income from other programs or with operating dollars.

## Operating Environment

- Seventy-one percent of respondents reported increased demand for services this year, up from 60 percent last year. Forty-two percent say increased demand is significant.
- Many respondents said that increased demands have been accompanied by a decreased likelihood that clients can pay for services.
- Health and social services agencies were most likely to experience increased demand (82%), as were small nonprofits (77%).
- Fifty-six percent of organizations with increased service demands said they were able to meet them. Only 35 percent of safety net organizations reported that they could meet increased demand.
- Forty-four percent of respondents expect that they will continue to see increases in demand next year. Fifty-seven percent of safety net organizations say they will not be able to meet next year's expected increases in demand.
- Seventy percent of respondents say that their cost of doing business has increased as a result of the recession. Commodity and fuel prices and changing regulatory environments are two contributing factors. Unlike in the for-profit world where prices cover costs and eventually produce profits (or a company goes out of business), nonprofits provide services that will never be profitable. Labor-intensive work, a necessary lack of economies of scale, and the inelasticity of prices (e.g. low-income uninsured people simply can't afford the cost of services, and third-party payers won't cover them either) contribute to this.

## Funding

- Forty-six percent of respondents lost an established funding source in the last year and 58 percent received reduced funding from a long-time funding source.
- Respondents lost funding from each major category of funding: 27 percent from foundations,

29 percent from government agencies, 24 percent from corporate funders, 25 percent from United Way, and 22 percent from individual donations.

- Twenty-eight percent of respondents that receive government funding do not receive timely contract payments or reimbursement for services already performed, leaving them to essentially “float the government” when their own operating budgets are skeletal.

## Strategies for Sustainability

- All respondents described strategic attempts to reallocate resources, reduce costs, and strengthen their fundraising programs. Areas in which respondents reported the most cuts were travel expenses (51%), salaries (42% plus 18% reported reduced fringe benefits), and professional development (40%).
- Forty-three percent of respondents partnered with another organization to provide programs and 39 percent increased their volunteer programs.
- Thirty percent of respondents reduced or eliminated programs or services. Thirty-nine percent of respondents added new programs or services or expanded existing ones in response to increased or changing demands.
- Respondents indicated that in the coming year their survival tactics would include more organizational partnerships, increasing earned income, diversifying revenues, and using more volunteers.
- In response to the downturn, many respondents requested additional funds from existing funders, requested special/emergency funding from new funders, requested advances on grants, requested that restricted funds be released for operating expenses, and sought guidance and advice from funders regarding program and operational strategies.
- Forty-four percent of organizations said that one or more funders provided additional funding in response to the downturn. Respondents also reported that some funders guaranteed that their funding would be maintained, talked to other funders on their behalf, and/or provided consulting or technical assistance.
- Thirty-eight percent of respondents reported that their Boards increased their fundraising efforts (including their own giving), 37 percent said that Boards participated in scenario planning, 14 percent said that their Boards tried to help but were not effective, and 27 percent said their Boards did nothing to address the crisis.

## Moving Forward

The most effective solutions nonprofits found for stabilizing their budgets and continuing to deliver their programs include:

- Refocusing fundraising efforts on new and different funding sources and approaching funders with a new message of urgency.
- Re-evaluating growth plans, analyzing program economics, and controlling costs through salary cuts and other reduced expenses.
- Board engagement in scenario planning and fundraising, targeted communications efforts, hiring management consultants to help revise business models and strengthen Boards, and advocating for legislative change.

The most critical issues facing respondents as a result of the recession include:

- Funding shortfalls and the uncertain nature of nonprofit funding.
- Cash flow problems due to rising costs, growing demands, and insufficient operating capital.
- Staffing-related challenges, including shortages, layoffs, low salaries, and stress and overwork.
- Unmet capital needs such as facilities repairs and expansion.
- Maintaining services in the face of growing needs and demands.
- Regulatory changes that make it more difficult to provide services.
- The need for capacity building and strategic change.

## Conclusions

Although there are some signs that the rate of declining revenues is slowing for nonprofits, the rate of increasing demands for service has not slowed and does not show signs of slowing.

- The bleak state of government budgets and the lag time related to foundation payout requirements are also likely to prolong the effects of the recession for nonprofits beyond the more general economic recovery.
- Nonprofit leaders have keener awareness of the precise ways in which the recession is affecting their organizations than they did last year. Many have made significant progress in implementing specific management solutions that helped to stabilize their operations.
- Many nonprofits are finding that cutting programs is the most important means to protecting their mission-critical work.
- Small and mid-sized organizations are generally facing more financial challenges than larger ones.
- Health and human services organizations are experiencing more financial challenges than nonprofits in other fields, most likely due to increasing service demands.
- Late government payments and the uncertain and short-term nature of foundation funding both hinder nonprofits' ability to deliver on current demand and to plan for the future. There is a need for improved, streamlined government payment systems and for longer-term and less restrictive grants and investments from foundations if nonprofits are to be resilient in the face of turmoil.
- The need to strengthen infrastructure and build management capacity through investment in training and development, quality administrative systems, communications, strategic planning, and technical assistance is often overlooked in times of crisis, but is more important now than ever.

We welcome your questions and feedback on this report:

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# I. Introduction

When the recession began in late 2007 the nonprofit sector almost immediately began feeling its effects. State budget crises, foundation endowment plunges, corporate profit losses, the bottoming out of credit markets, and the personal financial declines of private donors coalesced into an abrupt drop-off in nonprofit support. At the same time, nonprofits on the front lines—those providing health care, housing, food, and other basic necessities—were hit with dramatically increased demands for their services.

Rising costs and falling savings, unemployment, foreclosures and bankruptcy, and the loss of health insurance coverage have continued to strain the nonprofit safety net over the last two and a half years. In a study of the Mid-South nonprofit community published by the Alliance in July 2009, sixty percent of respondents reported experiencing increased demands for their services. According to *Downstream and in Demand*, three-quarters reported decreased revenues and half expected to end their fiscal year with a budget deficit. Not surprisingly, respondents reported losing funding from all major categories of funding sources, including government grants and contracts, foundation giving, corporate support, and individual donations.

A year later, the Alliance has taken another reading of the local nonprofit sector in an attempt to determine what has changed and how. *Downstream and in Demand II* found local nonprofits continuing to take it on both sides. Although some of the quantitative data shows a slightly rosier picture, it's clear that the sector is continuing to struggle with revenue losses and overwhelming demand. Some organizations that felt fairly protected from the first wave of the recession are only recently beginning to see their earned income fall off or their multi-year grants not renewed. Still others are seeing the longer-

term effects on their constituents, such as those who have stopped receiving unemployment or health benefits and those who were foreclosed on after a long effort to keep their homes.

Once again we also found remarkable evidence of the talent and commitment of the local nonprofit sector in rising above the recession to meet their missions. This report is intended not only to demonstrate how nonprofits are affected by the economic crisis but what they're doing about it. Nonprofit leaders have continued to find creative solutions to increase their impact with even fewer resources. Most solutions are not without difficult decisions and sacrifices—staff layoffs, program cuts, holding off on urgent capital needs. Through our network of more than 1,000 organizations, we have seen an impressive array of brave, innovative, and effective responses to keeping afloat in these rough waters.

Thanks to the 146 nonprofit leaders that participated in this study, we can provide an up-to-date snapshot of how local organizations are faring in the current climate, what they are doing to adapt and overcome the challenges, and the critical issues and needs that must be addressed if their essential role is to be protected. Although their funding may be discretionary, nonprofit organizations are not an option. They're a cornerstone of our community charged with providing thousands of lifeline services and raising the money to pay for them. This report is intended to help funders, public officials, and other nonprofit stakeholders to further understand the depth and breadth of the impact of the recession on local nonprofits, and to invest in their vital role during the current challenging times and for years to come.

## Overview and Background

The U.S. nonprofit sector includes more than 1.5 million organizations, employs more than 15 million people, represents more than ten percent of the nation's workforce, and accounts for almost 12 percent of its GDP. In the Memphis metropolitan area there are more than 3,000 nonprofits, and an additional 900 congregations and religious organizations classified as nonprofit. Nonprofits account for approximately eleven percent of the region's 60.6 billion dollar economy.

The country's nonprofits saw charitable donations from foundations, corporations, and individuals decline by 3.2 percent in 2009, according to [Giving USA](#), after dipping 2.4 percent in 2008. Health, human services, arts, education, and environmental organizations were most affected, with giving down approximately ten percent in each field, although giving to health, human services, and environmental organizations did improve somewhat in 2009.

Charitable giving by Memphis-area donors was about 1.6 billion dollars in 2007, with 80 percent of these dollars going to local organizations. According to *Downstream and in Demand*, almost three-quarters of local nonprofits lost funding from corporate funders and more than 60 percent each lost funding from foundation grants, individual gifts, and major gifts in 2009.

## Methodology

**Survey.** A 40-question survey was developed and published via the web-based SurveyMonkey software in June 2010. The survey was posted on the Alliance website and publicized in newsletters and through direct emails to the Alliance nonprofit membership. Questions were multiple-choice and open-ended. There were 130 eligible responses.

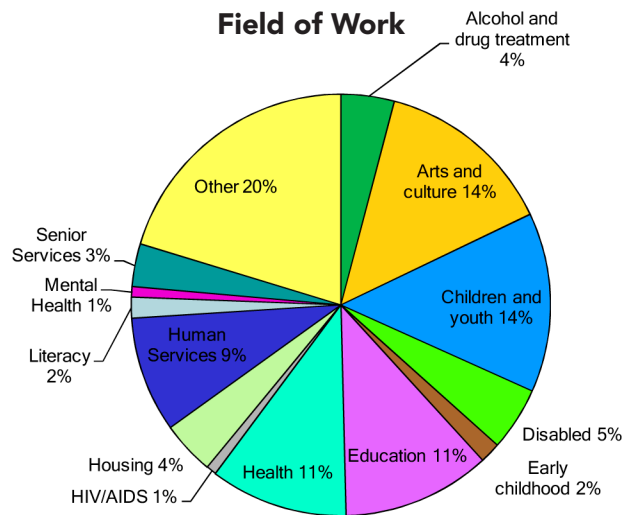
**Focus Groups.** Three focus groups were held in June 2010. Sixteen nonprofit leaders participated, representing diverse fields including education, health care, arts and culture, youth services, and various others. Participants were asked six to eight questions related to how the down economy has affected their organizations, how funders have responded, and what they see as their most critical organizational needs and issues. Responses were transcribed and feedback and comments are included throughout this report.

**Confidentiality.** All participants in this study were assured complete confidentiality.

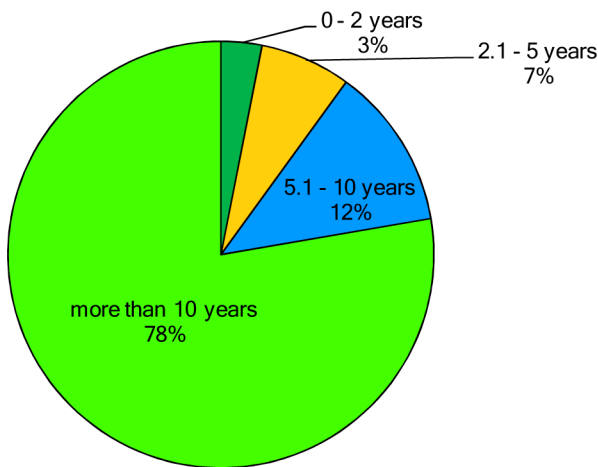
# II. Participants at a Glance

## Field of work

Survey respondents represent organizations in the fields of arts and culture (14%), children and youth services (14%), health and health care (11%), education (11%), and human/social services (9%). A combined total of 22 percent of respondents work in alcohol and drug treatment services, services for the disabled, early childhood, HIV/AIDS, housing, literacy, mental health, and senior services. Twenty percent of respondents work in diverse other fields including economic and community development, homelessness, public safety and crime prevention, legal services, and environmental conservation.



## Years in Operation



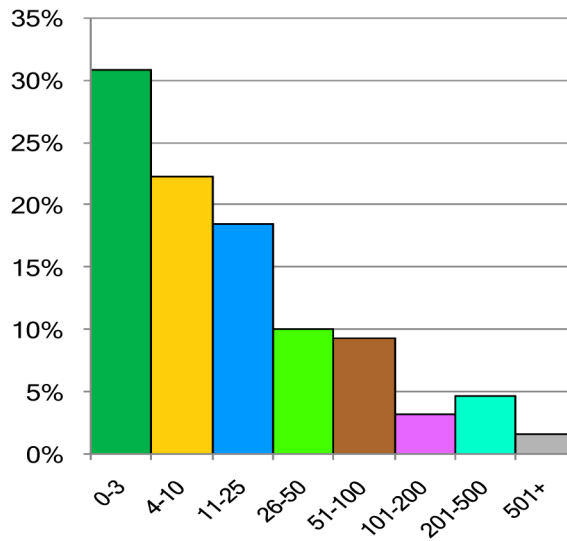
## Years in Operation

Seventy-eight percent of organizations represented in the survey have been in operation more than ten years. Twelve percent are between five and ten years old, and ten percent are less than five years old.

## Staff Size

Fifty-two organizations (27%) represented have three or fewer staff and 43 (22%) have four to ten staff members. Approximately 35 percent have between ten and 100 employees, and 17 percent have at least 100 employees.

## Full Time Staff



## Safety Net Organizations

Safety net organizations are those that provide programs or services that serve critical needs regardless of clients' ability to pay, especially in emergency situations. Communities and local governments depend on safety net organizations such as hospitals and health clinics, homeless shelters, and food pantries, to meet these needs. Twenty-eight safety net organizations took part in the survey, representing 22 percent of respondents.

## Budget Size

Respondents represent organizations with a wide range of operating budgets. Approximately half have budgets of 1 million dollars or below, 28 percent are in the mid-size range of 1 to 5 million dollars, and 23 percent have budgets of over 5 million dollars.

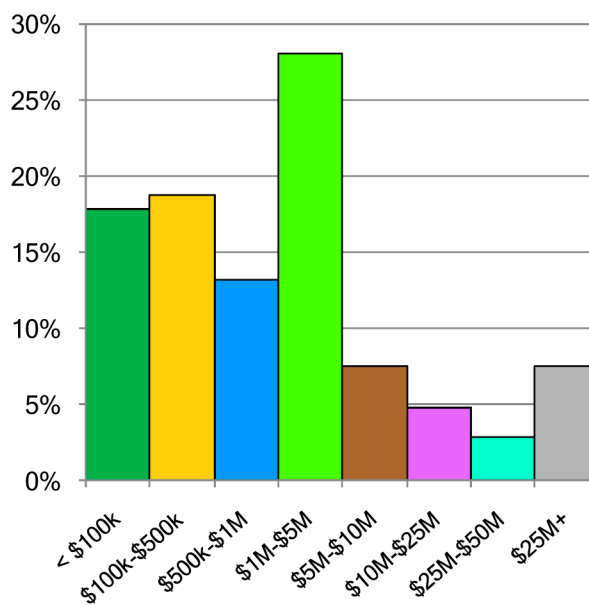
## III. Financial Trends

Nonprofits have taken a beating since the country's economic downturn began. Funding cuts, budget deficits, and a bleak financial outlook were major themes of last year's findings, and this year's study reflects continued financial stress across the board. There are indicators that financial stability is improving for many organizations, but it's important to take into account the severe cuts and low performance most experienced in prior years—many nonprofits had nowhere to go but up. Declines might have slowed, but for many organizations it will take at

## Organizational Title

This report reflects the responses of those who occupy senior leadership roles in Mid-South nonprofits, which include mostly Executive Directors, Chief Executive Officers, and Chief Financial Officers. A small number of respondents are Associate Directors or have other job titles, including Vice-President, Development Director, Operations Manager, and Project or Program Manager.

Total Revenues



least several years of increasing revenues to return to pre-recession levels.

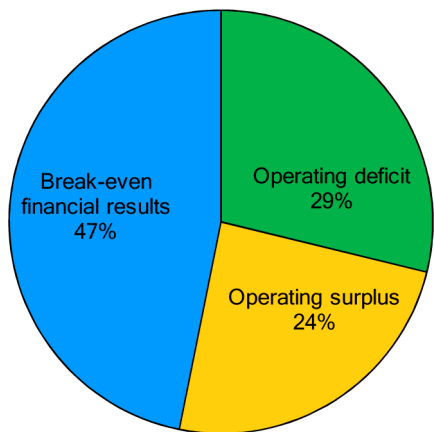
Further, comparatively positive revenue trends do not necessarily reflect a more advantageous operating or funding environment. Increased revenues between the current and previous years must account for the numerous restructuring, fundraising, and operating and programmatic planning efforts nonprofits have conducted to stabilize their organizations and programs despite continuing or worsening conditions.

## Revenue Trends

Twenty-nine percent of respondents indicated that their revenues have stayed at approximately the same level between fiscal years 2009 and 2010. Twenty-one percent saw their revenues rise by up to ten percent during this time. Although about 16 percent saw revenue increases of more than ten percent, more than a third of respondents—35 percent—experienced revenue declines since last year.

These findings contrast sharply with last year's survey, when 73 percent of respondents indicated that their revenues had declined since the previous year. Of those who reported a decrease between fiscal years 2008 and 2009, half indicated that the decrease was more than 20 percent of total revenues. This year, only 20 percent of those with decreases reported these as more than 20 percent.

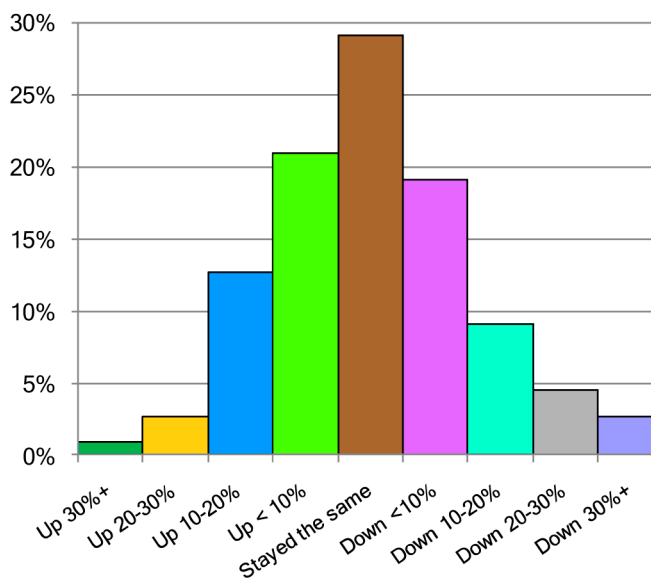
### Expected FY 2010 End-of-Year-Status



Small organizations (those with revenues under one million dollars) were the hardest hit by revenue declines. Only a quarter of larger organizations (those with revenues over ten million dollars) experienced declining revenues, but 40 percent of small organizations reported declines.

Thirty-two percent of mid-sized organizations (those with revenues between one and ten million dollars) saw declines. None of the largest organizations reported that their revenues had declined by more than 20 percent. In one quarter

## Changes in Revenues, FY 2009-2010



of the small and medium-sized organizations with declining revenues the decline represented more than 20 percent of total revenues.

## Budget Deficits

Twenty-nine percent of respondents indicated that they would end the current fiscal year with an operating deficit, down from 49 percent last year. Twenty-four percent indicated they expected to end the year with a surplus and 47 percent expect to break even. Thirty-percent of small organizations and 29 percent of mid-sized organizations expect to end the year with a deficit, as opposed to only 13 percent of large organizations. Local figures are lower than national ones: in the U.S. 35 percent of nonprofits ended last year with an operating surplus.

Forty percent of organizations expecting a deficit say it will be between 20,000 dollars and 100,000 dollars, and 18 percent expect a deficit of more than 100,000 dollars. Although we might expect deficit size to correspond to budget size, medium-sized organizations reported the largest deficits: 92 percent say their deficit will be at least 20,000 dollars, whereas no large organizations expected a deficit of more than 20,000 dollars. Twenty-four percent of small organizations say their deficit will be at least 20,000 dollars. Safety

net organizations appear to be expecting among the largest deficits: of the roughly third of safety net organizations expecting a deficit, 80 percent expect it to be at least 20,000 dollars.

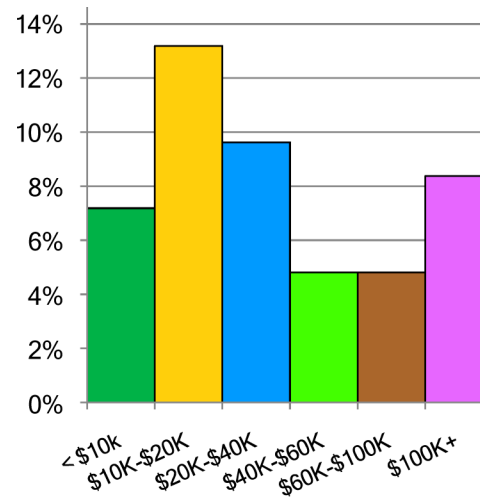
## Cash Reserves

Nonprofits need to maintain cash balances that are sufficient to support payroll and operations as well as pay for unexpected expenses. Different organizations may need different levels of cash on hand, depending on their revenue structures (e.g., those with regular cash income from contracts or programs might not require as much as those that rely on fundraising.) All organizations, however, require some cash to cover shortfalls and maintain a cushion for unanticipated shortfalls.

Fourteen percent of respondents indicated that their organizations have no cash reserves, compared to 27 percent last year. Approximately 34 percent have one to three months of reserves, 39 percent have four to twelve months, and 13 percent have at least one year. In last year's study, only one percent of organizations reported having cash reserves of more than a year. This year 13 percent say they have at least a year of reserves. These figures also compare favorably to national figures: a study by the Nonprofit Finance Fund found that only 39 percent of respondents have more than four months of reserves.

As might be expected, small organizations are least likely to have cash reserves. Forty percent of small organizations say they have less than a month of reserves, compared to 21 percent of medium organizations and 20 percent of large organizations. Less than a quarter of small organizations have more than six months of reserves, compared to 53 percent and 40 percent among medium-sized and large organizations, respectively. Safety net organizations are also less likely to have cash on hand—41 percent reported having no more than a month of reserves available.

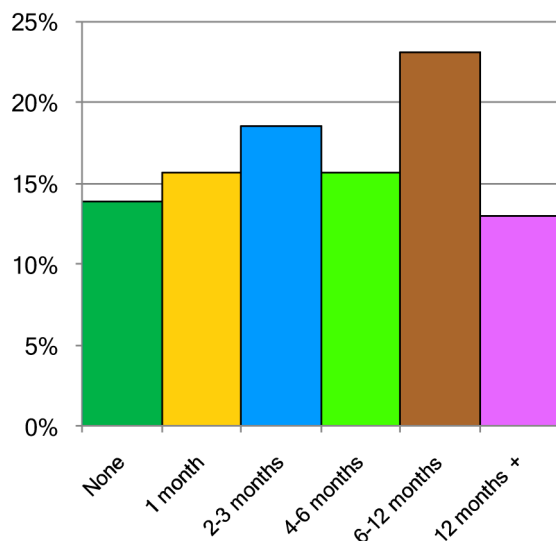
**Expected End-of-Year Deficit, FY 2010**



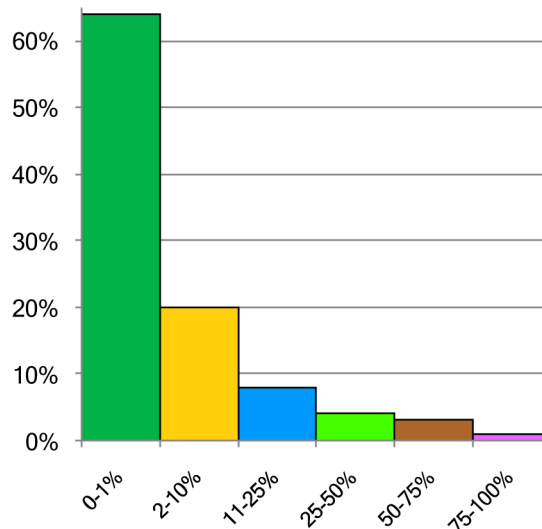
Cash Reserves	Small orgs	Medium orgs	Large orgs	Safety net orgs
0-1 month	40%	21%	20%	41%
More than 6 months	23%	53%	40%	20%

Sixty-four percent of respondents that have cash reserves have spent no more than one percent of their reserves. Twenty-eight percent have spent up to 25 percent, four percent have spent between 25 and 50 percent of their reserves, and another four percent have spent more than 50 percent.

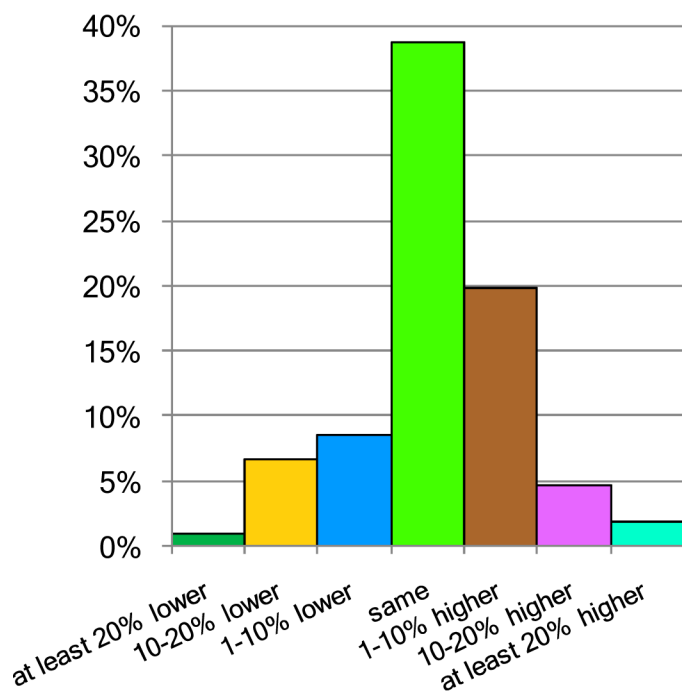
### Available Cash Reserves



### Cash Reserves Spent



### Change in earned income, FY 2009-FY 2010



### Earned Income

Respondents were asked about trends in their earned income, which includes revenues generated from programs, services, products, and membership fees. Fifty-nine percent of respondents say their organizations have maintained earned income at the level of the previous year or increased it by up to ten percent. Six and a half percent have seen earned income grow more than ten percent. Sixteen percent indicated that their current year's earned income has dropped off. Mid-sized organizations saw greater drop-offs in earned income than large or small organizations, at 30 percent.

Many respondents remarked on the effects of the economy on demand for their services. One leader of an organization that provides back-to-work programs remarked that loss of earned income was directly tied to the for-profit sector, as demand for workers had fallen among its corporate partners. Others mentioned seeking new ways to increase earned income, such as renting space, charging fees for previously free services, or holding events. Some respondents indicated that although they had not yet increased earned income, they had set specific goals to do so in order to offset decreased grant funding.

## Credit

Forty-eight percent of respondents reported applying for a line of credit in the past year in order to stabilize their finances, and 48 percent reported receiving a line of credit. Nationally 30 percent of nonprofits reported that they had applied for loans and 74 percent received them.

Twenty-eight percent said they maxed out a line of credit in FY 2010. Large organizations were more likely than mid-sized and smaller organizations to apply for credit, possibly because of greater capitalization needs or because they had more experience with debt financing. Large organizations were also more likely to qualify for credit, and less likely to max it out. Eighty percent of large organizations applied for credit, compared to 33 percent of mid-sized nonprofits and 50 percent of small nonprofits. Sixty percent of large organizations that applied for credit were able to obtain it, compared to 50 percent of mid-sized organizations and 37 percent of small organizations. No large organizations reported maxing out credit, but 42 percent of mid-sized organizations and 25 percent of small organizations did.

The tightening of the credit market has made it both harder for nonprofits to get credit and more expensive to do so. Banks have withdrawn from nonprofit lending less because of high risk than because of low transaction profitability. Larger organizations may be more likely to have larger asset bases to leverage debt and to seek larger loans that meet lenders' profitability requirements.

## Overall Financial Position

Sixty-four percent of respondents say they will be in a better overall financial position at the end of the current year than the previous year. Many commenters attributed this to cutting expenses "to the bone," and limiting program costs and "non-essentials." Some pointed out that their financial improvements are not without costs, citing layoffs and increased workloads for staff. A handful of respondents reported that major attention to fundraising will have put them in a better place than last year.

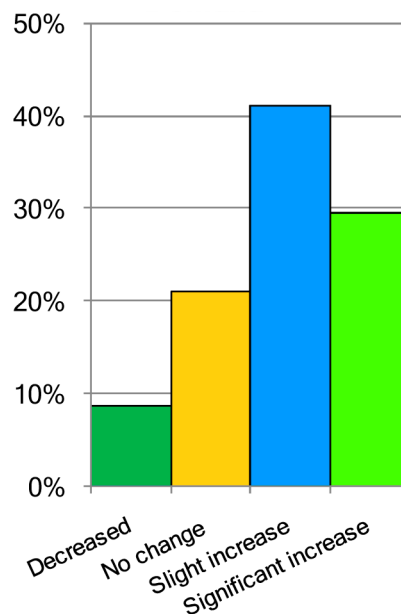
# IV. Operating Environment

## Demand for Services

As more people face unemployment, foreclosures, cuts in benefits, and rising transportation costs, they turn to nonprofits to help meet basic needs such as food, shelter, and health care. For the last several years, Mid-South agencies, especially health clinics, food pantries, and others on the frontlines, have reported rising demands for their services.

Seventy-one percent of respondents reported increased demand for services this year as a result of the economic crisis, up from 60 percent between fiscal years 2008 and 2009.

Change in Service Demand

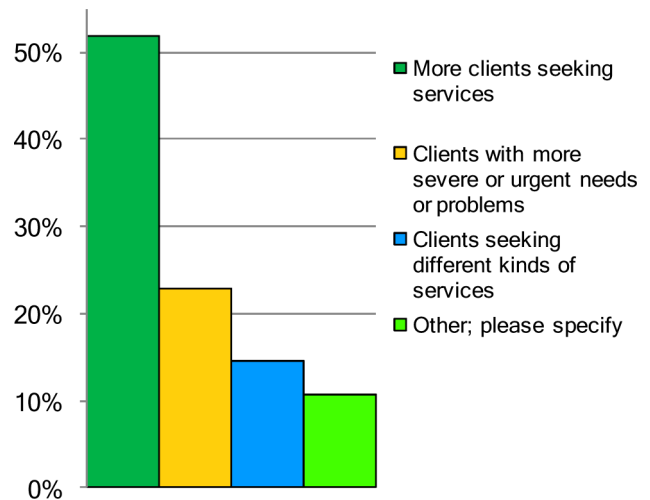


Of these, 42 percent described the increased demand as significant. Among health and social services agencies, 82 percent were likely to experience increased demand, and 78 percent of safety net organizations reported increased demands. Seventy-seven percent of small organizations and the same percentage of mid-sized organizations reported increased demands, compared to 57 percent of large organizations. Many respondents said that increased demands have been accompanied by a decreased likelihood that clients can pay for services.

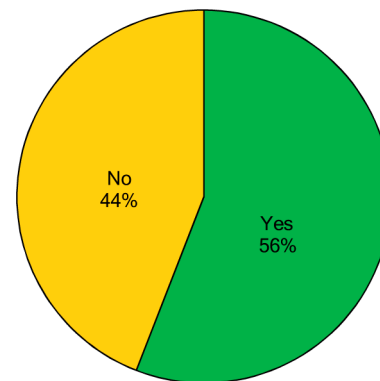
Participants were also asked about the nature of their increasing service demands. The most reported type of increased demand is a greater number of clients seeking services. Sixty-two percent of respondents reported client increases, 28 percent reported that clients present with more severe or urgent needs and problems, and 17 percent say clients are seeking new or different services. According to one health clinic which previously served only low-income, inner-city residents, corporate layoffs have led to "more people from Germantown, Collierville, and other middle-class areas" coming in for services.

Fifty-six percent of organizations that reported increased service demands said they were able to meet them. This number was lower for health and social services organizations (53%) and only 35 percent of safety net organizations reported that they could meet growing demands.

### Type of increased demand



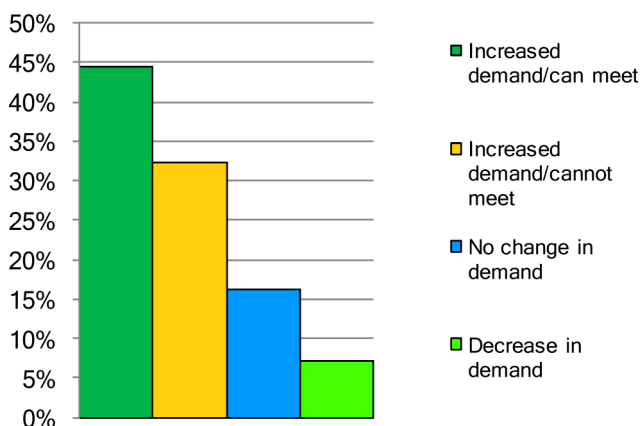
### Able to meet demand for services?



Numerous respondents described having to start or expand waiting lists. Several mentioned that they didn't have enough staff to meet demands, and others described how staff experience and training were insufficient to serve needier clients.

Asked about expectations for next year, 44 percent said they expected continued increases in demand for their services that they will be able to meet, and slightly more than 32 percent indicated they expected increases that they would not be able to meet. More than 57 percent of safety net organizations said they will not be able to meet increases in demand.

### Able to Meet Demand FY 2011



## The Flipside: Falling Demand

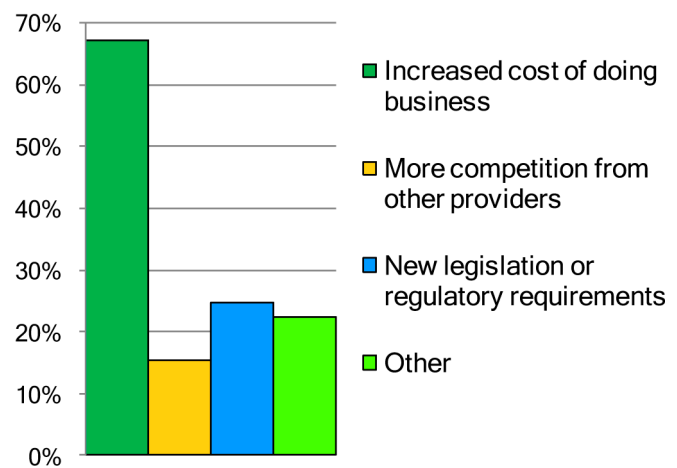
For some organizations it is *decreasing* demand that indicates clients and supporters are struggling. Elective programs such as those in the arts, environmental organizations, and private schools and after-school programs are pointing to decreased enrollment, lower ticket sales, shrinking memberships, and other signs of the recession. Many of our best-loved arts institutions, those that reflect and represent the culture and quality of our region, are the first ones to be overlooked in times of hardship. Schools and other programs that provide educational alternatives and serve special populations also find themselves not making the cut. One private school leader said that since the recession began parents are more likely to transition their child to public schools than they used to, and that lack of scholarships has caused enrollment declines.

## Operating Environment/Other Aspects

In addition to rising service demands, many nonprofits have seen their whole operating environments change as a result of the recession. The increased cost of doing business was named

by almost 70 percent of respondents as a key recessionary challenge, with some pointing specifically to food and transportation costs. Legislative and regulatory changes related to funding, accreditation, and client eligibility have impacted about a quarter of respondents, particularly those in health and mental health. Increased competition from other providers was also named as a factor by some, as were membership losses due to individuals cutting costs, technological changes, and a variety of social and community-level factors.

Changes in Operating Environment



## V. Funding

### Funding Trends

Every nonprofit funding channel has been affected by the recession. Individual gifts, foundation grants, corporate support, and government funding streams all slowed at the first sign of crisis, and have continued to remain low for several years. Many respondents told stories of long-time donors dropping off, pledges deferred, grants not renewed, and contracts suspended.

Forty-six percent of respondents reported losing an established funding source in the last year and 58 percent reported receiving reduced funding from a long-time funding source. For some

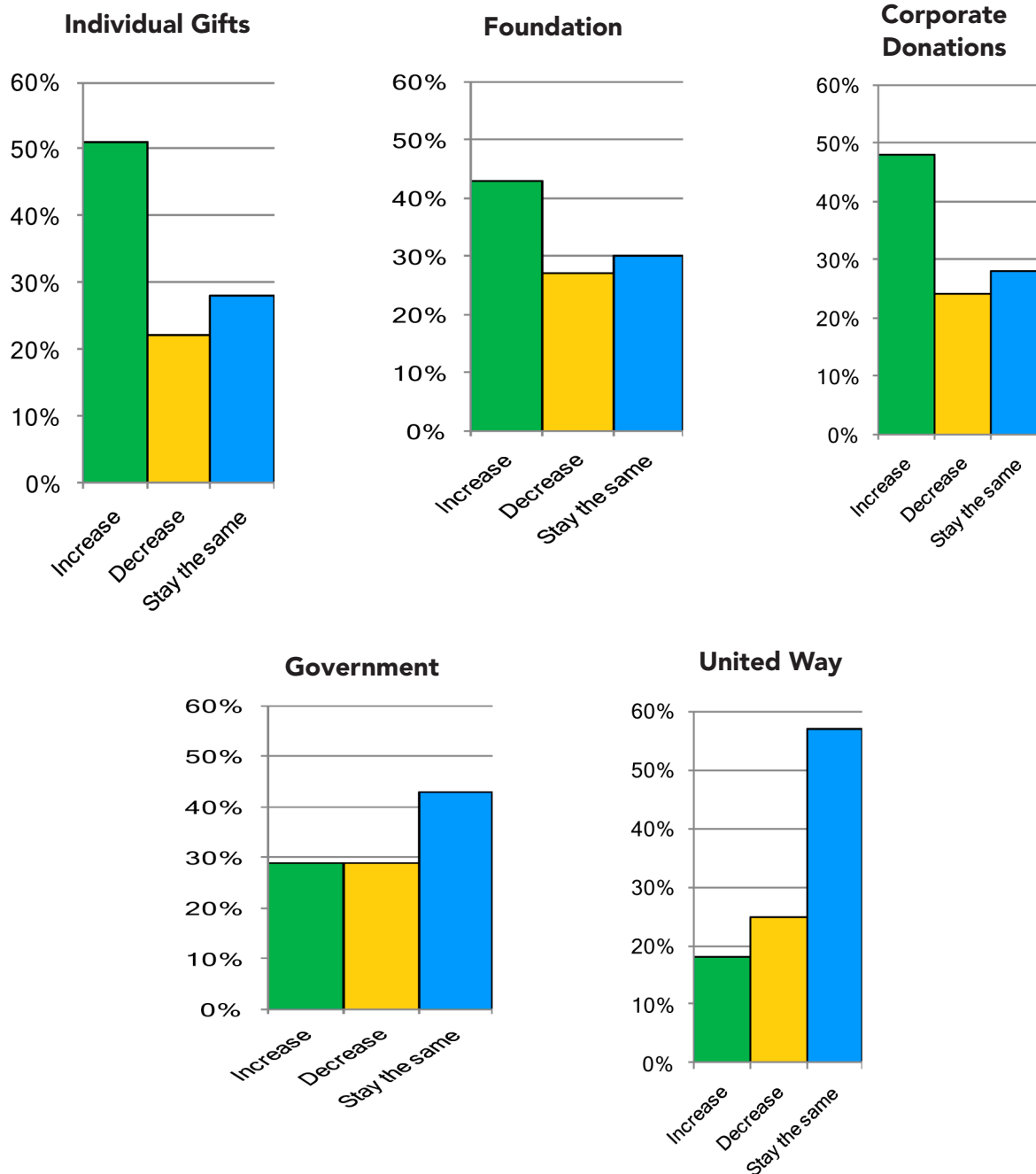
the loss of one major donor was significantly damaging; for others it was the loss of numerous smaller donors—one respondent reported losing 14 of 15 donors, each of whom gave about \$10,000 annually. Still others reported that although they did not lose donors, their donors were cutting back from multiple-year to single-year commitments.

Respondents were also asked about the extent to which different categories of funding are expected to decrease or increase. Funding decreases appear to have dropped off since last year, when respondents noted decreases in corporate sponsorships (70%), corporate grants

(69%), major gifts (62%), foundation grants (61%), small individual gifts (57%), and special events (50%). This year 29 percent of respondents saw decreases in government funding, 27 percent in foundation funding, 25 percent from United Way, 22 percent in individual giving, and 24 percent in corporate gifts.

Respondents also reported expecting increases in funding from each type of funder, including 51 percent in individual gifts, 48 percent in corporate support, and 43 percent in funding from private foundations. Experts say that it

will be a while before funders fully rebound, especially foundations that have seen their endowments shrink. Foundation responses have varied, from freezing programs to eliminating one or more funding cycles to decreasing the amounts funded or the number of grantees. As one participant noted, "We have taken a noteworthy hit in foundation and corporate funding, as most have scaled back giving. Even with markets/ investments rebounding slightly, lingering uncertainty about the future dictates funding decisions..."



## Restricted Funding

Restricted funding may be used only for specific programs or projects and typically limits the amount of funding that may be used for overhead. Restricting funding has been common practice among funders in recent years, primarily as a means of increasing grantee accountability and the trackability of their investments. Many nonprofit experts are critical of program-restricted funding, believing it prioritizes spending over social impact. General operating funds provide flexibility and allow nonprofits to be more responsive to changing conditions.

Last year's survey found that restricted grants were a key challenge for respondents, who said that flexible funding is even more critical during a time of financial setbacks. Again this year, respondents reported insufficient operating budgets and the need to invest in management capacity, and suggested that working capital to increase financial flexibility is crucial if they are to act strategically in the current environment.

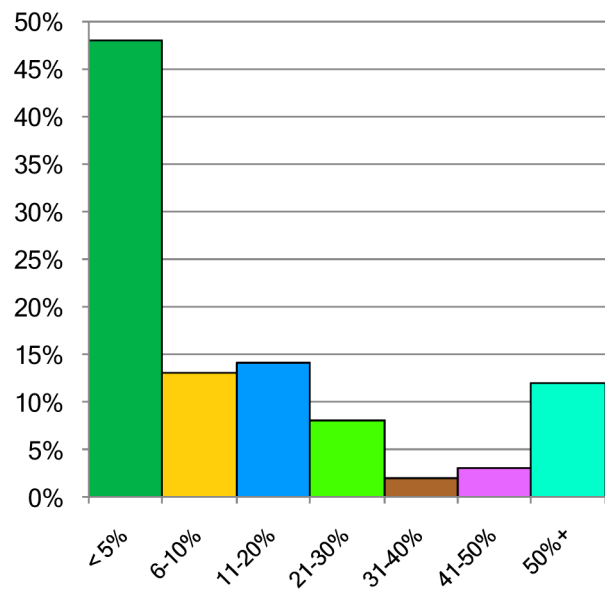
Forty-eight percent of respondents reported that less than five percent of their funding is restricted. Thirty-five percent said that between six and 30 percent of their funding is restricted, and 17 percent said that more than 30 percent is restricted.

## Government Funding

Respondents were asked if and how government grants and contracts had been affected by the recession in the last year.

Twenty-eight percent of respondents that receive government funding say that they do not receive timely contract payments or reimbursement. Some commented that county, city, and/or state agencies were frequently late with reimbursements, and several noted cash flow problems as a direct result. Said one participant, "We've seen a slowdown in city payments...[we're] now waiting at least six weeks to get paid" and another described waiting "eight to nine months on the County...at one time we were owed \$500,000." Another, describing

Restricted Funding



how a contract that was supposed to begin in July took until October to get signed, said "we're financing the government."

Nineteen percent say that their government funders have imposed stipulations in the last year that reduce how much their organizations get paid. These include automatic withholding of funds and discounts for early payment. Given the rising costs of doing business, late payments and limited reimbursements have doubled the challenge for many. Several respondents pointed out that even if per-unit payments increase with service demands, most government contracts do not pay for the accompanying increased administrative and capital needs.

According to some, government funding is not worth the administrative requirements. One participant said his organization took on a Federal contract to increase revenue, which was nothing but "a total pain in the neck...the cost to administer it far exceeded the benefits."

Twenty-eight percent of respondents were recipients of American Recovery and Reinvestment Act (ARRA) funding. Although some described the funding as a helpful infusion of funds for a specific objective, several respondents commented that the one-time nature of these funds presented a challenge. Eighty-two percent say that when the money is spent, their organizations will be unlikely to replace the funding from other sources.

# VI. Strategies for Sustainability

## Survival Tactics

Respondents were asked to describe what their organizations have done this year to overcome challenges brought on by the economy. Many described strategic attempts to reallocate resources, reduce costs, and strengthen their fundraising programs. Areas in which respondents reported the most cuts were travel expenses (51%), salaries (42% plus an additional 18% said they reduced fringe benefits), and professional development (40%). Forty-three percent said they partnered with other organizations to provide programs and 39 percent said they increased their volunteer programs. More than a third of respondents reported adding new programs to meet increased demand or as part of a restructuring process, and almost a third said they reduced or eliminated programs or services. Thirty percent conducted scenario planning and 25 percent held more Board meetings to discuss challenges and plan their strategies. A quarter of respondents said they diversified funding revenues and 23 percent increased earned income.

Respondents were also asked about their planned responses for next year. The most frequent answer was "Partner with other organizations to provide programs," at 44 percent. Increasing earned income, diversifying revenues, using more volunteers, expanding programming, and scenario planning were also ranked high.

Strategies Implemented, FY 2010	
Reduced travel expenses	51%
Partnered with other organizations to provide programs	43%
Frozen hires and staff salaries	42%
Reduced training and professional development expenses	40%
Added or expanded programs	39%
Increased volunteer usage	39%
Stayed more on top of receivables	36%
Reduced or eliminated programs/services	30%
Developed scenario plans	30%
Held more frequent board meetings	25%
Delayed payments to vendors	25%
Diversified funding revenue	25%
Increased earned income	23%
Reduced fringe benefits	18%
Partnered with other organizations to reduce administrative costs	14%
Postponed a fund drive or capital campaign	13%
Worked remotely	10%
Changed your mission and/or vision	8%
Re-negotiated a lease	7%
Sold assets	6%
Asked a funder to unrestrict current funding	6%
Merged with another organization	2%

Future Planned Strategies	
Partner with other organizations to provide programs	44%
Increase earned income	37%
Diversify our funding revenue	33%
Increase the number of volunteers your organization uses	32%
Add or expand programs	27%
Stay more on top of receivables	27%
Develop scenario plans	25%
Reduce travel expenses	22%
Freeze hires and staff salaries	21%
Reduce or eliminate programs/services	18%
Reduce training and professional development expenses	14%
Hold more frequent board meetings to share reports and look at the financials	14%
Partner with other organizations to reduce administrative costs	13%
We are not doing any of the above.	13%
Lay off staff	9%
Delay payments to vendors	8%
Reduce fringe benefits	7%
Sell assets such as a building or securities	5%
Change your mission and/or vision to better respond to the economic conditions	5%
Worked remotely	5%
Re-negotiate your office lease	4%
Ask a funder to change a restricted grant to unrestricted funding	2%
Postpone a fund drive or capital campaign	1%
Merge with another organization	0%

## Layoffs

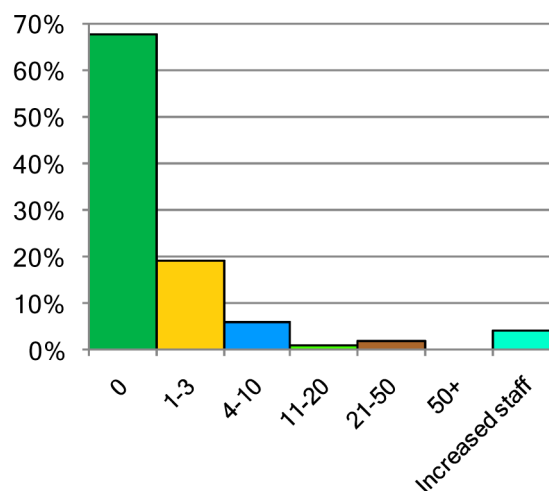
Respondents were asked about the number of staff members they let go this year as a direct result of the economic crisis. Sixty-eight percent said they did not have to make layoffs. Twenty-five percent laid off between one and ten employees, and only three percent said they had to lay off more staff. Four percent of respondents reported increasing their staff size in the last year.

## Funder Relations

The recession has thrown many foundations into turmoil as well as their grantees. Many of the country's largest and wealthiest foundations have severely cut programs, staff, and giving levels in order to stabilize and regroup. The foundation community has encountered criticism from those who believe that they are hoarding their wealth

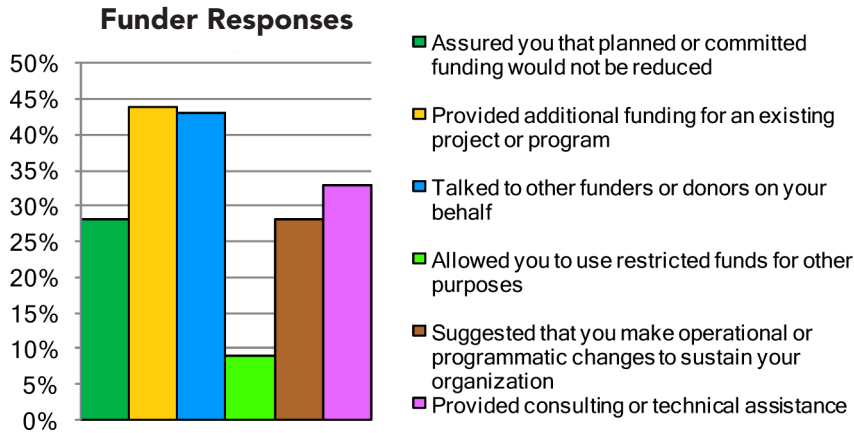
and guarding assets rather than helping grantees when it is most needed. The desire for more information from and better communication with funders was expressed more than any other theme in last year's survey.

**Staff Layoffs**



This year we were curious to learn if and to what extent funders have taken this message to heart. Forty-four percent of respondents said that their funders provided additional funding for an existing project or program, and 43 percent said that a funder talked to other funders or donors on their behalf. Thirty-three percent said

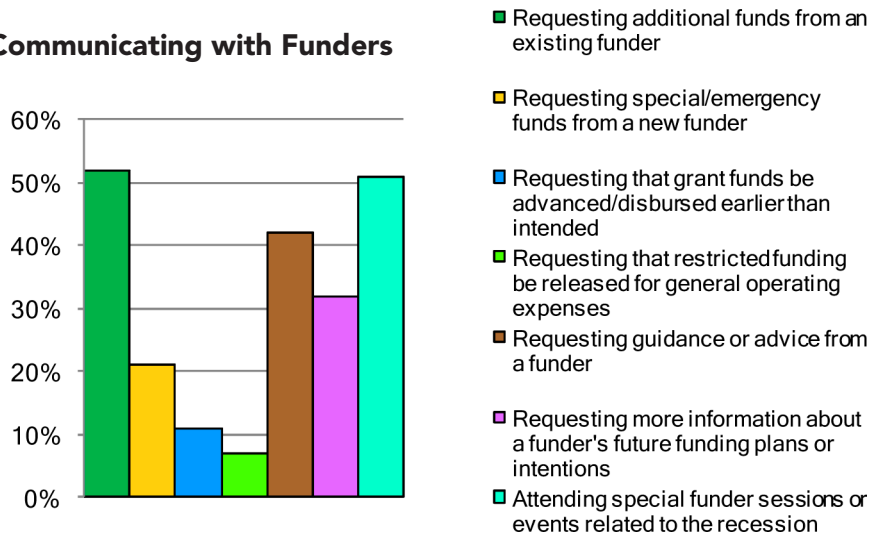
that funders provided consulting or technical assistance and 28 percent reported that funders advised on operational or programmatic changes. Twenty-eight percent were assured by a funder that their funding would not be reduced, and nine percent said that a funder allowed them to free up restricted funding for other needs.



Respondents were also asked about the steps they took to communicate their needs to funders. Just as funders have been called on to be honest and strengthen their commitments to grantees, nonprofit leaders are also responsible for expressing their needs and cultivating effective relationships with funders.

Fifty-two percent of respondents said they approached their funders for additional funding, 42 percent said they requested guidance or advice from a funder, and 32 percent said they requested more information about future funding plans.

### Communicating with Funders



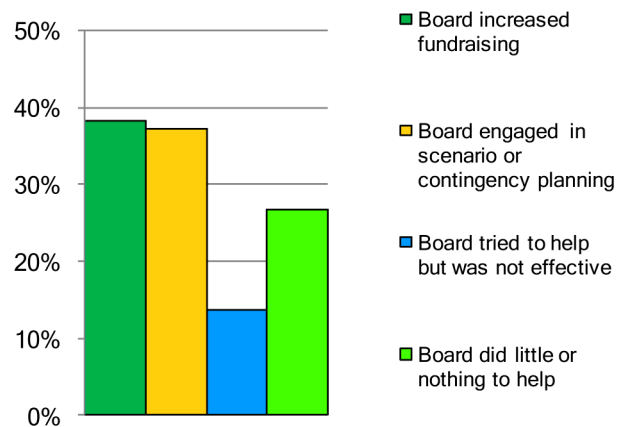
## Board Roles

Respondents were asked to describe the role played by their Boards of Directors in helping their organizations through the economic crisis. Thirty-eight percent reported that their Boards expanded or intensified their fundraising efforts in response to the recession. Some, however, expressed frustration that “the Board isn’t interested in fundraising.” Thirty-seven percent said that their Boards conducted contingency or scenario planning in order to systematically look at what conditions will be like down the line, assess the risks and opportunities, and develop systematic plans based on these future outlooks.

Several respondents commented that their Boards focused mostly on financial monitoring, and that their Boards became more involved in fiscal management. One organization described how the Board decided that it could not meet its fundraising goals and thus elected to dissolve the organization. Although many respondents praised their Boards—“phenomenal,” “focused

on the long-term,” “gone beyond committed”—some suggested that more involvement was not necessarily valuable involvement. Fourteen percent of respondents said that their Boards tried to help in some way but were not effective, and 27 percent said their Boards did little or nothing to address the crisis. Said one Executive Director that has seen a “real difference” in the Board since the recession began, “of course, 30 percent are still doing all the work.”

### Board Responses



## VII. Moving Forward

Nonprofit leaders have been coming together with their staffs, Boards, advisors, and peers to identify and implement realistic approaches to getting through the current crisis. They have relied on honest communication and rigorous organizational self-analysis to assess and address their risks, and have taken bold proactive steps to strengthen their programs and operations. When asked to name the most effective steps taken by their organizations to navigate their options and mitigate the effects of the recession, many gave detailed examples of management decisions, investments in fundraising, cost-cutting, and collaborative partnerships that have stabilized their budgets and kept their programs intact. The variety of responses to this question was impressively diverse, as shown by the following comments:

### Fundraising

**Many organizations refocused their efforts on new and different funding sources and**

**approached their current funders with a new message of urgency. Tactics included:**

“increasing our donor base”

“establishing a fundraising position for the first time”

“increasing sponsorship solicitations”

“increased attention to larger donors”

“running both a capital and an annual fund campaign”

“writing new proposals to corporations”

“providing incentives for donor-advised funds”

“getting REALLY creative about increasing revenue”

“focusing more on small donors”

“changing the focus of our earned income programs to fit the present economy”

## Financial Management

**Respondents reported re-evaluating their growth plans, analyzing program economics, and making budget cuts to balance their budgets, including:**

- “controlling costs, negotiated reduced pricing”
- “reducing operational expenses” and “tightening budget”
- “cutting salaries” and “freezing salaries”
- “conducting more financial projections, comparative trends, closer look at operating budget”
- “agency-wide restructure, minimized staffing, reduced benefits, implemented emergency fund”
- “controlling expenses—much better money management”
- “reducing programs that were not cost-effective”
- “reducing non mission-critical expenses”
- “reinventing business model”

## Other Steps

**Respondents reported an array of other approaches have helped them take steps toward stabilization and improved their organizational outlooks:**

- “Board developed very specific plan with goals and timetables”
- “Merger with another organization”
- “Partnered with another organization which led to receiving unexpected grant funding”
- “Communicating our position to constituents very clearly”
- “Community relations”
- “Advocating for legislative changes”
- “Consulting led to Board training and development”
- “Strategic planning”
- “Being honest” and “Adhering to our mission”

## Critical Issues

Respondents were asked to describe the most critical issues facing their organizations as a result of the recession.

Respondents were most likely to describe **fundraising challenges** as their biggest threat. In addition to funding shortfalls, respondents cited donor fatigue, reliance on grants and other “uncertain” sources and lack of steady funding stream, late payments, and the difficulty of being in a field that is a “tough sell” for funders.

**Cash flow**, including rising costs, unexpected expenses, and insufficient operating capital, was also frequently mentioned. Many respondents said that funding administrative and overhead costs was their greatest challenge. Price swings for needed supplies and equipment including food and fuel were frequently named. Lack of viable funding sources, late payments by donors, and investment income swings were also mentioned as major threats to stability.

**Staffing-related challenges**, including shortages, layoffs, low salaries, and overwork/stress were also common responses. Salary freezes and cuts in staff and benefits were among the most frequently mentioned urgent problems, especially among those with the critical need or potential to grow. Although many praised their staff commitment to organizational survival, effects on morale and organizational culture were common themes: “Staff is fatigued,” “workload has been absorbed by those [who are wearing too many hats],” “no raises in three years has led to low morale,” “Our ED had to ask for a sabbatical...and still needs some time.”

**Capital needs** were another urgent issue:

“Space...not enough to admit more participants, nor the means to build or renovate,”

“deteriorating buildings,” and “delays in maintenance and renovation” were common themes.

Many respondents replied that **field- and social-level changes**, and a current or potential lack of capacity to respond to them, were their most pressing concerns. “Maintaining service levels

in the face of escalating costs” was commonly mentioned, because “more and more families need services but can’t pay,” and “needs are [still worsening...people have] lost jobs and insurance and are struggling to pay for medications, transportation, other basic needs.”

In some cases the changing landscape was linked to a **changing regulatory environment**. Many respondents mentioned the potential impact of health care legislation as a major problem. “Effects of proposed changes in state law,” “change in regulatory environment,” and “new office holders with changing focuses” were cited as key challenges. Several respondents suggested that decision-makers are out of touch with changing issues and needs. According to one, the most pressing need is “to educate and facilitate further change in the paradigm.”

A final theme for many respondents was the imperative for broad-scale **strategic change** within their organizations. “Operational

assessment,” “planning,” and “growth strategies,” were described as urgent needs, and several mentioned that only a complete “overhaul” or “restructure” would save their organizations. According to one respondent, the only remaining course of action is “deciding whether to merge or close.”

Finally, several organizations stated that their greatest organizational challenges were not a direct result of the recession. Whereas the tough economic climate may have exacerbated the challenges, many nonprofits had existing systemic weaknesses, e.g., lack of internal controls or do-nothing Boards, before the recession began. As one respondent wrote, “our most pressing problem stems from within.” For some, the economic crisis has actually “made us stronger,” “made us creative,” “made us cautious,” “changed our mindset,” “helped us renew our culture,” and “fortified our mission.”

## VIII. Reflections/Conclusions

Respondents wrote and spoke thoughtfully about their experiences and perceptions of the impact of the recession on their organizations and their fields. Some key themes that emerged include:

**1. Continued challenges.** For many organizations, the recession has been unrelentingly challenging, with no sign of improvement in the last year. This is especially true for many lifeline organizations working in health care and social services. Other respondents conveyed that they are only recently being impacted by the downturn. Although they initially felt the recession would not deeply impact their work, the current fiscal year has brought new funding losses, hits to earned income, regulatory challenges, and increased clients and service demands.

**2. Honing in.** One of the biggest differences between last year’s survey and this one was

the number and diversity of specific strategies implemented not only to respond to the downturn, but to prepare for expected future challenges. Last year respondents spoke much more vaguely about skyrocketing demands and the overwhelming pressure to make budget cuts. This year, many nonprofit leaders reported more understanding of precisely how their organizations have been or will be affected.

**3. Not sitting still.** Many respondents reported that in the last year their organizations were able to pull out of initially devastating circumstances. They conveyed that although they did not feel “in the clear,” they had made progress in identifying and implementing specific management solutions that put them on the path to survival.

**4. Pulling programs.** One of the strongest themes to emerge was the urgent necessity to address programmatic priorities. Respondents

reported getting much more aggressive about understanding which programs are most central to their missions, which are running deficits, and which are subsidizing other programs. Many nonprofits have cut programs without reliable sources of revenue in order to protect their most mission-critical work.

**5. Size and vulnerability.** In general, small and mid-sized organizations are contending with the most financial instability. This could be because large organizations are more likely to have well-established systems and designated staff for financial analysis, because they have greater financial assets allowing them access to credit, and/or because they have more program areas and funding streams allowing them a greater flexibility of options for change.

**6. Safety net threat.** Health and human services nonprofits that provide critical programs for low-income people are faced with the most severe threats to financial stability, primarily because they have seen the most dramatic increases in service demands. This year service demands continued to rise as more households faced the loss of jobs, housing, and health coverage. Because a higher percentage of health and human services organizations rely on government contracts, regulatory changes, decreased funding, and delayed reimbursements have exacerbated the problem.

**7. Undermined by late payments.** Local and state budget crises have forced government agencies to impose late payments on nonprofits. Contracts that are held up and overdue invoices have caused major cash flow problems for many respondents. Organizations with already bare-bones budgets are being asked to float the government for services when they are already suffering financial shortfalls and struggling to keep up with increasing demand.

**8. Too many surprises.** Although some respondents reported unexpected windfalls such as unsolicited grants and surprise donations, many others reported unanticipated cuts. Even those organizations that conscientiously

conduct scenario planning face uncertainty about their futures. The nature of short-term, one-time, and open-ended funding is especially challenging when nonprofits are operating on a shoestring. Although some funders made initial announcements about their intentions when the recession first hit, many have not sustained the communication. Nonprofits continue to ask for more multi-year funding, larger and less restricted grants, and program- and market-related investments. As nonprofits come to funders better adapted to the current climate and with specific strategies in place, they are ready for long-term commitments and partnerships to help them meet expectations.

**9. Earned income not for everyone.** Many respondents reported looking for new sources of earned income or adjusting their current revenue structure to focus more on earned income. However many experts say that nonprofits overestimate demand and underestimate administrative costs when launching new earned income programs. Pricing, programs, and products must be carefully analyzed to ensure that earned income is truly worth the investment.

Studies show that nonprofits with more earned income tend to weather the recession better. However, this conclusion doesn't account for the fact that those organizations likely to see the greatest service demands—health and social service organizations—are also those for which earned income is least likely to be appropriate. While boosting earned income is a savvy strategy for many organizations, it's not an answer to the long-term investment in the social safety net that nonprofits are charged with maintaining.

**10. Infrastructure and management capacity still top needs.** All economic times require nonprofits to conduct sound financial planning, manage with an eye to the future, and adapt to changing needs. But in unstable times the need for capacity building and systemic improvements becomes vital. Nonprofit leaders still feel that funders, although they may pay lip service to capacity building, have not fully embraced the

crucial reality of what one respondent called the need for “hunker-down money.” Many respondents say they have held ground and even strengthened their organizations as a result of investment in training and development, quality administrative systems, communications and marketing, strategic planning, and consulting and technical assistance. Now is not the time, they say, to focus on quick superficial solutions.

**11. No finish line.** Although there’s much talk about the recession being on its way out, there will be no immediate relief for most Americans or for most nonprofits. Even if the stock market is improving, the damage done in many communities will be long-lasting. Further, although jobs and spending will gradually increase, the nonprofit recovery will lag behind the national recovery due to depressed giving rates, lost investments, continued state budget crunches, and foundations’ three-year rolling payout averages. Many nonprofits have downsized, merged, closed, or changed scope

or direction, and we can expect a long period of resettling even as economic conditions improve.

**12. Increased visibility for the sector.** Under the current Presidential administration a new interest and expressed commitment to nonprofits has taken hold. Although recent Federal efforts to invest in the nonprofit sector have met with controversy, we can expect that efforts to bring nonprofits into a more visible and influential role in the nation’s economy will continue. At the same time skyrocketing interest in social enterprise is helping to spur interest in the potential of nonprofit innovation from private investors. Although neither front is likely to change the day-to-day struggles for a local shelter or after-school program, nonprofit leaders hope for a trickle-down effect in awareness of their impact and for increased support for replication, expansion, and new research and ideas. For this to happen, however, nonprofits must also carefully invest in education, engagement, and advocacy that help them claim their place at the table.

### Thank you

The Alliance would like to thank all those who gave their time to participate in surveys and focus groups. Their cooperation has enabled us to assemble this snapshot of the Mid-South nonprofit sector in the ongoing recession.

In addition to helping funders and policymakers better understand how nonprofits are faring, we view our research as an important tool to expand and improve our services as a support organization. Sharing the experiences and perceptions of our members helps us to strengthen our own role in advancing the viability and impact of nonprofits in our beloved community.

We would also like to express our appreciation and thanks to Elizabeth Sachs, who compiled the survey results and wrote this report.

We welcome your questions and feedback on this report:

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