SOUNDING BOARD

PERSPECTIVES ON NONPROFIT STRATEGIES FROM WOLFBROWN

v. 24

THIS ISSUE FEATURES:

A special issue devoted to gaining perspective on the challenges and opportunities facing nonprofit organizations in this extraordinary time of economic stress and volatility.

Navigating Troubled Waters

Many of our clients and friends are understandably worried about the likely effects of the economic downturn. They report much conflicting advice, confusion, and disagreement among stakeholders. What will be the impact on foundation grants? Private giving? Earned revenues? What is the responsible way forward for management and board leadership?

In the past few weeks, we have spoken with CEOs who do not foresee any disruption of business as usual, and others who are in panic mode. We have spoken with funders whose assets are not compromised, and others who have put a moratorium on new grants. The outlook from state and local agencies is grim.

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Just how long the economy will remain in recession is anyone's guess, and the impact on donations and consumption patterns is a matter of conjecture at this point. We believe that most nonprofit cultural organizations will see at least a moderate drop-off in private giving, especially large gifts from individuals, as well as a moderate to severe drop-off in corporate and foundation support. The impact on earned revenues may also be significant, as discretionary spending contracts.

Our senior consultants have been discussing and debating what sort of guidance would be most helpful in this time of extraordinary volatility. Rather than provide you with a prescriptive list of "dos and don'ts," we prefer instead to offer a more expansive view. Tom, Joe, Laura and Alan offer independent perspectives from their unique vantage points, each arguing for a somewhat different approach to navigating troubled seas.

We all agree that surviving the next two years will require significant focus on planning, increased structural flexibility and capacity to adapt quickly, willingness to take risks and innovate, a new openness to collaborating, and a heightened responsiveness to community need.

Is There a Silver Lining?

Dr. Thomas Wolf

You remember all of them, don't you? The major recessions of 1980-1982, 1990-1991 and 2001-2002? You don't? Well, you needn't feel bad. None of the other people I talked to in the last few weeks – people old enough to have lived through these times – could remember them either.

As a consultant, my memories are different because our firm has had to help clients in both good times and bad times. We opened our doors in 1983, immediately following the 1980-1982 recession. Reagan had cut the federal budget, which hit nonprofit organizations especially hard. At the same time, many states were reeling from taxpayer revolts. State appropriations were down and local economies (and nonprofit organizations) were hurting. Our clients initially struggled to adjust, but times got better fairly quickly. This pattern was repeated during and after the recession of 1990-1991.

Many have said that the economic downturn that began in 2008 will be different than earlier ones. They say it will be more severe, last longer, and have a permanent debilitating effect on nonprofits.

Perhaps they are right. This recession appears to have had greater global reach, the volatility of the financial markets seems unprecedented, venerated financial institutions have failed, and the amount of money being injected into the banking systems of many countries speaks to the structural seriousness of the problems.

Yet if history is any guide, those who are responsible for the health and vitality of nonprofit organizations should channel their concern away from impulsive and panicked action and toward thoughtful analysis. This may be an opportune time to look hard at mission and make thoughtful and deliberate decisions about priorities. Yes, there will inevitably be pain. But the evidence is that organizations that stay true to their missions in difficult times, ask hard questions about how well they are serving constituents, make contingency plans, and think carefully about how to be more competitive and effective are the ones that not only survive but thrive in the years of prosperity that inevitably follow.

Consider Silicon Valley, a region that undertook community cultural planning in the late 1990s. The plan included many optimistic proposals for regional initiatives, only to be thwarted by the bursting of the tech bubble after 2000. Cultural Initiatives/ Silicon Valley used this as an opportunity to focus on a single priority activity – arts education – which had been supported by over 90% of surveyed citizens a few years before. That laser-like focus led to an enduring program of sustained growth and improvement in the schools over the ensuing years.

Or consider the response to economic difficulty in a small town about four hours north of Silicon Valley, where an enlightened group of citizens saw an opportunity for several small struggling organizations (ranging from natural history to forestry to the arts) to create something that was more than the sum of their parts and that would help them realize their missions of serving the public more effectively. Good planning led to the merger of these five entities into what is now Turtle Bay Exploration Park, a 200-acre campus that has become a tourist destination on the Sacramento River and an institution that provides broad service to the community.

Perhaps the lesson is that bad times do not last forever. And good planning in bad times can inevitably lead to good decisions that will have positive ramifications for the long term.

Tough Questions, Disciplined Answers

Joseph Kluger

Since mid-September, when the financial crisis became widely apparent, I have asked arts leaders how deep they think it will be and how long it will take for endowment asset values – and those of our donors – to return to last year's levels. Much like the volatility of the stock market, I hear conflicting answers from many seasoned board and staff leaders. While no one knows for sure, in my view, the majority of economic pundits are probably correct in saying that the recession will be longer and deeper than anything since 1973-1974 (which very few of today's arts leaders experienced professionally).

This economic downturn is also having an impact on some of the underlying principles that guide the way arts groups will operate in the future.

The rapid demise of some of our most venerable commercial institutions is a signal to our societal psyche that institutional history and a sterling reputation do not guarantee survival. With the fall of big companies like AIG, Merrill Lynch and Lehman Brothers, the message for arts groups is that longevity and high artistic standards alone are not enough to ensure sustainability. For arts leaders and funders, the challenge will be recognizing that constant uncertainty and an accelerating pace of change requires shifting our mindset from developing long-term strategic plans to creating a culture of short-term "constant planning."

Although I have no definitive answers

for navigating these uncharted waters, I urge arts leaders to reach internal consensus on disciplined answers to some provocative questions – in light of present circumstances, not past experiences:

- **Mission:**
  - o Does our mission still serve our needs and those of our community of supporters?
  - o What systems do we have in place to understand the relevance of our mission to the community, and how it might be changing?
  - o Are there other nonprofits in our community whose missions overlap ours (in whole or in part), with whom we can explore an alliance?
  - o How do we define and measure success in achieving our mission?
- **Programs:**
  - o Do all of our programs really serve our mission? Are we disciplined in using "artistic quality" and "community relevance" as rationales for supporting only those programs that generate measurable progress towards our mission?
  - o Which of our current programs are so valuable that, if we were not doing them now, we would add them even in these challenging times? Are we prepared to eliminate those that do not meet this test?
  - o Which new programs are so innovative and compelling that we will add them, whether or not we have incremental funding? Are we prepared to reallocate resources from existing programs or fixed costs, to invest in these new programs?
  - o Are there ways to decrease the program planning timeline, so that the scope of programs can be adjusted to meet actual resources?
- **Customers:**
  - o What can we do to attract and retain audiences whose personal finances may also be stretched?
  - o How can we "hard-wire" an audience feedback mechanism into our operations to ensure that we are always being responsive to our customers?
  - o How can we maintain our institutional presence in the marketplace with limited marketing resources? Are there opportunities for marketing collaborations with other arts groups or better trade deals with media outlets?
- **Finances:**
  - o Are there ways to reduce fixed costs, or turn fixed costs into variable costs, without compromising the mission?
  - o Are we operating as efficiently as we can? Can we share administrative functions with other nonprofits?
  - o Can we increase our working capital, or build a contingency into our operating budget, in anticipation of unpredictable budget variances?
  - o Do our performance measurement systems enable us to adjust plans rapidly as needed?

I have confidence in the inherent value of arts and culture to make our lives better, especially in times of great stress. But, this is not a sufficient value proposition, on its own, to get through these challenging times. I do not mean to suggest that arts leaders should make wholesale changes indiscriminately. What is needed is a disciplined, ongoing process of evaluating goals, strategies, programs and financial plans in light of these uncertain and constantly changing times. There must also be recognition that staying the course, or retrenching to core programs, will not be enough to weather a long recession. Visionary leaders will also use the challenges as an opportunity to pursue creative, strategic alternatives and to invest in innovative solutions wherever possible.

Laying a Strong Foundation

Laura Mandeles

The New York Times reported in September that the Starr Foundation, a large shareholder in AIG, lost $1 billion from its portfolio. While this may be an extreme example, many foundations are likely to curtail grantmaking over the next few years. As with the last shock to the philanthropic sector after 9/11, the current crisis may also lead to more fundamental changes in giving priorities.

Many foundations base their grants on a three-year rolling average of their endowments, so the effects of the current decline may take a year to hit, but could last for several years. However, Kathleen Enright of Grantmakers for Effective Organizations is recommending that GEO members consider continuing this year's grant levels into next, even if it means paying out more than five percent. The impact on corporate giving is likely to be particularly significant, especially in geographic areas hard hit by mergers, acquisitions and company failures. In the public sector, city, county, and state governments are experiencing severe budget challenges, due to dropping real estate values and sales taxes. And, of course, individuals are looking at devalued holdings in the stock market.

The overall picture suggests a significant contraction in philanthropy. Gifts to capital campaigns will be more difficult to secure, and there will be fewer gifts of appreciated securities for tax reasons at the end of this year.

Nonprofit organizations on *The Chronicle of Philanthropy*'s "Philanthropy 400," a list of the largest recipients of charitable contributions, are seeing pledges go unfulfilled, decreases in donations from donors of modest means, and skyrocketing operating costs as more people seek services.

In thinking about how to tackle the situation proactively, I suggest that resource development executives consider a number of strategic and tactical initiatives:

- Big dreams should not be abandoned, but this is a time for nonprofits to focus on meeting ongoing needs and budgets, lengthening timeframes for achieving capital goals, and "looking lean" to funders, while still making the case for their long-term vision, as well as their short-term service.
- Organizations must demonstrate that they are using scarce funds wisely and efficiently, and that their financial controls and planning are tight and realistic. Information about cost-saving steps should be a part of communications to donors. Increased levels of accountability will be demanded, and the most successful nonprofits will get ahead of this curve.
- More, not less, communication is necessary in times like these, rallying core donors to their leadership role in getting the organization through tough times, stewarding donors of planned gifts, and reinforcing to all donors and prospects the importance of their commitment at whatever level is feasible.
- Development staff will have to run harder to stay in the same place. This is the wrong time to cut back on staff charged with research, donor stewardship, and grant writing.
- This would be a good time to press forward on adopting a culture of fund raising throughout the organization, so that every contact, event, and activity is analyzed and developed for its fund-raising and friend-raising potential.
- Now is an opportunity to lay a strong foundation for a diverse funding base in the future, so that when the economy turns up again, the staff, board, strategies, and structures are in place to take full advantage of available resources.

Most importantly, I see this as a good time to question fundamental assumptions about why the organization exists and how it can be sustained in the long term. The case for funds is only as strong as the underlying core values, aspirations and operating plans of the institution. People come together in times of crisis. If you can harness this energy and bring leadership together to re-evaluate mission, constituencies, programs, governance, and staffing, you will gain a deeper level of buy-in among your stakeholders and ultimately strengthen your position to emerge as a stronger and more relevant institution.

Burning Down the House

Alan S. Brown

Financial distress quite naturally engenders a conservative response. Batten down the hatches, revert to core programs and protect the *status quo* at any cost. Isn't that the responsible thing to do?

As we enter this financial downturn, many nonprofit cultural institutions are chronically under-resourced, over-extended on fixed costs, over-reliant on a few donors and have a long history of walking a financial tightrope with no safety net. Very few engage in meaningful contingency planning. Most do not have explicit policies for managing artistic risk, and few have cash reserves set aside to weather normal fluctuations in demand and support. That we have come to such a high level of vulnerability should hardly surprise anyone.

As the tightrope unravels over the coming months, many arts groups will defiantly tighten their grip on the remaining threads of their financial model, while others will welcome the opportunity to weave a new rope.

Which will be your pathway?

Many important strides forward emerge from crisis, for good reason. The first stage of any change process is the realization by all stakeholders that things must be different in the future. Significant change is simply not possible while the belief persists that the *status quo* is an achievable outcome. I love to ask arts managers what they would do if their facility burned to the ground unexpectedly. With this license to re-imagine, many are relieved to have a blank canvas and are filled with imaginative ideas for how to emerge stronger than ever.

But why must we wait for the house to burn down in order to create meaningful change?

In a healthy cultural ecosystem, there is natural growth, fierce competition for resources, and regular dying and regeneration. We do a pretty good job at growth and competition, but it's the regeneration part that concerns me.

This is an ideal time to start thinking seriously about new models for regeneration. We need a better playbook for endings. Mergers and other forms of creative alliances should be vigorously explored. New ways of auditing institutional performance on non-financial outcomes like intrinsic impact need to be developed so that we can better assess public value. Maybe we even need a new receivership program – a way of transitioning distressed nonprofits – to become "the third option" between bankruptcy and painful downsizing, much like an elderly parent gives durable power of attorney to a child.

At WolfBrown we have been discussing the need for a new sort of planning process – one that culminates in reinvention – when consensus is reached that the *status quo* is not an option. But such a process is all but impossible to manage while simultaneously squeezing ever harder on the existing business model. Different sides of the institutional brain are at work.

Imagine that a nonprofit board votes to dissolve the corporation on a future date and to re-incorporate as a new entity with a fresh start the following day. Half the board is charged with managing an elegant ending. The other half is charged with re-imagining what is possible, unencumbered by existing conditions. Dying is considerably more appealing when, like the proverbial phoenix, new life emerges.

The real crisis, then, is not financial stress but unfocused leadership, outdated business models, and planning methods that do not address the range of possibilities for dramatic change. In this time of uncertainty and accelerated change, board members and staff must honestly and openly discuss the moment in time at which protecting the *status quo* becomes counterproductive.

Elegant endings and thoughtful transitions are successful outcomes, not failures. So, go ahead, burn the house down. Adversity is a necessary springboard to paradigmatic change and a vibrant future.

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