A Guide to Navigating the Recession

An FAQ for the Nonprofit Sector

What is the difference between a downturn, a recession and a depression?

Downturn: a short-term decline in economic activity.

Recession: a significant decline in economic activity spread across the economy, lasting more than a few months. Traditional indicators include real Gross Domestic Product (GDP), real income, employment, industrial production and wholesale-retail sales. The National Bureau of Economic Research (NBER) ultimately decides whether the economy has fallen into recession. **The start of a recession can only be seen in the rear-view mirror.**

Depression: a longer, more severe recession. It is loosely defined as an economic downturn where GDP declines dramatically, usually by more than 10%.

When did this recession begin?

On Monday, December 1, 2008, NBER announced the United States had been in recession since December 2007.

Why is this recession different?

The severity and length remains in question, but this is only part of the story. We are plagued by a combination of events we haven't seen in any of the market events over the past 20 years:

Credit markets have seized up

Stock market plummeted

Employment has fallen in many sectors

Housing construction and real estate markets declined

Many state unemployment funds are borrowing from the federal government; welfare and Medicaid may be close behind.

What is the impact of recession on the nonprofit sector?

Nonprofit Finance Fund (NFF) has completed two studies of nonprofits in recession. NFF analyzed 6,500 mid-sized nonprofits through the 2001 recession to understand how these organizations were affected. NFF's study found that both during and after the 2001 recession, more nonprofits experienced deficits than before it began. In 2005, the number of nonprofits experiencing deficits was still greater than before the recession began. Additionally, nonprofit expenses outpaced revenue during this time.

In early 2009, NFF surveyed over 1100 diverse nonprofits across the country and found that America's nonprofits are financially vulnerable.

Only 12% of all respondents expect to operate above break-even this year.

Just 16% anticipate being able to cover their operating expenses in both 2009 and 2010.

31% don't have enough operating cash in hand to cover more that one month of expenses, and another 31% have less than three months' worth.

In 2009:

- 43% anticipate a decrease in funding from government
- 62% anticipate a decrease in funding from foundations
- 49% anticipate a decrease in funding from individuals
- 33% anticipate a decrease in earned revenue

52% of respondents expect the recession to have a long-term (2+ years) or permanent negative financial effect on their organizations.

93% of lifeline organizations that provide essential services anticipate an increase in demand in 2009.

Nonprofits are taking steps to weather the recession that range from cuts to essential programs to layoffs. When asked to identify actions taken within the past 12 months or planned for the next 12 months:

- 39% identified "reduce or eliminate programs"
- 41% identified "reduce staff or salaries"
- 23% identified "delay payments to vendors"
- 65% said "develop a 'worst-case scenario' contingency budget"
- 43% said "use reserve fund"

What does this recession mean to nonprofits and funders?

This recession could affect nonprofits and funders in multiple ways:

Immediate downward pressure on government, philanthropic and "discretionary" individual revenue sources

Limited and/or more expensive access to credit

Increasing demand for basic and critical human services

In early and out late - the nonprofit sector may have felt the recession early and it may take longer to recover due to foundations' 3-year rolling averages, depressed giving rates, state budget timing and the abundance of government contracts in the sector

What should my nonprofit consider doing during this financial crisis?

1. Nonprofit managers, board members and professional advisors can come together and review and optimize three critical aspects of a nonprofit's financial assets:
    - Cash deposit risk - is your money insured, or distributed among a number of banks?
    - Concentration of investment risk - are your investments diversified and varied?
    - Concentration of revenue risk - are you dependent on a particular revenue stream that might dry up?
2. Stay on top of revenue and expenses; re-evaluate your revenue projections on a regular basis and plan for expenses that reflect your revenue reality.
3. Engage in contingency planning with board members and funders on how to respond to higher demand for services. The goal is to ensure you stay afloat to serve the community. This may mean partnering with other complementary organizations.
4. Avoid large investments in fixed assets and infrastructure - e.g. a building purchase, new hires or expansion of services. To the extent possible, work with funders and the board to build a cash cushion to allow flexibility and course corrections.
5. If once reliable revenue sources seem questionable, consider ways to diversify, especially within your existing target market(s). But avoid over-diversification (i.e., new business lines) that can increase risk and cost structure.
6. If your organization offers services that will lessen the negative impact of a recession, approach government funders more aggressively for support.

    Download NFF's "Questions to consider in a financial crisis" for a self-assessment worksheet.

    Download NFF's "Tips on Navigating the Financial Crisis"for list of questions to help you assess and address risk for your organization.

What are the questions my nonprofit should be asking internally during this financial crisis?

In this economic climate, nonprofit leaders need to start asking themselves tough questions about program, finance and management.

Program:

What are our programmatic priorities?
What will current and prospective funders support?
How will our organization respond if there are not reliable sources of revenue (contributed and earned) for all programs?
How important to our mission are programs that are running a deficit?

Finance & Management:

Is financial and programmatic information available for management in a timely manner?
How accurate and agile is the decision-making culture?
Do management and board hold each other accountable for achieving agreed upon goals? Are responsibilities clearly stated?
Which programs contribute to the bottom line? Which need the most general operating support to "subsidize" the gap between total expenses and direct revenue?
Will there be an increase in demand for our services? If so, how will growth impact our fixed vs. variable cost structure?
What can we deliver currently and in the future without adding administrative or other fixed costs?
What is the cost of each additional client served?

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Is now the right time for my organization to think about a merger or an alliance with another nonprofit?

More and more, nonprofits are entering into alliances and mergers with other organizations to better fulfill a common mission. It's essential that nonprofits considering collaboration engage in thorough analysis and planning - from determining feasibility, to final implementation, to forecasting. NFF can guide nonprofits through every step of the process. Contact your local NFF office to begin a conversation.

For more information on nonprofit mergers and alliances, read "Merger Myths" in the April 1, 2009 NonProfit Times by NFF's merger and alliances expert, Tom McLaughlin.

How should my nonprofit handle a facility project during the recession?

Large investments in infrastructure and facilities can be riskier now that the economyis in recession. Many nonprofits are dealing with cuts in funding, increased demand for services and reduced access to capital. This is the time to approach facility projects with caution; that said, if a nonprofit is willing to make sure every "i" is dotted and every "t" is crossed, there are still smart ways to approach a facility project.

If you're planning a facility project...
Now more than ever it is crucial for organizations to thoroughly plan and prepare for a facility project.

Prioritize components of your facility project: What must get done and what could be phased in at a later date? What could be considered an "extra"? Now may be a good time to focus on the basics, and perhaps leave out some of the extra bells and whistles that are nice, but not necessary.

Plan for different scenarios - create alternative project plans based on the amount of funds raised. Before commencing the project, know how it will be fully financed.

In most markets, traditional financing options have decreased. Community Development Financial Institutions (CDFIs), like NFF, may be able to provide capital for projects.

If your project is in a low-income community and eligible, another possible source of capital is New Markets Tax Credits.

Build in higher contingency needs as donor pledges may convert at lower rates than in the past; your planning period may be longer so exposure to raw material price fluctuations may be greater.

Lending institutions are employing a more rigorous credit process so be prepared for a higher level of due diligence from lenders; the process of applying for a loan could take longer than in the past.

In-kind services may be more readily available from project managers, architects and others who are on the front lines of the slowdown in the construction market.

If you're in the midst of a facility project...
If you haven't already done so, prioritize components of your facility project.

If possible, chunk out the facility project in phases, focusing on immediate needs first.

Consider scaling back your project based on conservative revenue projections.

Don't be afraid to explore what would happen if you lost half of your funding - how would you modify your project?

In this economy, you may be in a position to renegotiate material costs and professional services pricing.

Be proactive about checking in with donors - reach out to them letting them know you are still going through with your project and communicate why their support is even more critical now.

What Actions Can Funders Take During the Recession?

NFF encourages funders to be active supporters of the organizations they care about.

Steps that can be taken include:

Ask grantees how you can best help them continue to deliver on the promise of their mission. Be aware of how your grant fits into the overall revenue picture for the organization, and fund at the 'enterprise' level. Consider how you might advocate on behalf of grantees, on anything from government funding policy to funder collaboration.

Avoid restrictions that compromise liquidity - unrestricted operating funds may be the best way to ensure organizations are able to continue providing vital programs.

Reduce the paperwork, stress and expense on grantees:

- Think in terms of "net grants" that take into account the cost of grant application and reporting.
- In the application process, ask only for what you need.
- Increase transparency around grant cycle timing and process.

The recession brings a long-standing problem into sharp relief: it reveals the precarious state of a sector that is continually asked to do more with less. This crisis presents funders and government with an opportunity to substantively change practices that perpetuate inefficiency and stymie innovation and growth. The talent, resources, and passion that people in the sector bring to the goal of addressing society's most pressing issues must be protected and nurtured. This recession is forcing the issue of how to better invest in what works for the benefit of society.

How can NFF help my nonprofit navigate this recession?

NFF has developed a continuum of services to help nonprofits manage through tough times, ranging from educational workshops to customized consultations that diagnose and address organizations' specific financial challenges. These services help managers better understand, interpret and use their financial data, so they can make and communicate well-informed financial and management decisions. Our critical juncture financing provides access to capital. All of these tools prepare nonprofits to make decisions in the short term that leave them financially sound for the longer term.

What online NFF resources are available to help my nonprofit manage through the recession?

Find an NFF recession workshop near you

NFF partnered with the Chronicle of Philanthropy to offer a web chat series "Financial Management in Tough Times". The web chats answered reader's specific questions on available financing, arts organization's business models, the role of foundations and raising money for capital campaigns in recession. Click here to read the transcripts of the web chats.

Download NFF tips for nonprofits in navigating the financial crisis

Download Questions to consider in a financial crisis - a self-assessment worksheet

Read the full results of NFF's Nonprofit Recession Survey

NFF President & CEO Clara Miller offers advice for nonprofits in the Chronicle of Philanthropy's online discussion "Weathering the Financial Crisis"

NFF's Clara Miller featured in the Stanford Social Innovation Review Blog: "Nonprofits Must Gear Up For Tough Economy"

As the Nonprofit Sector Faces Recession, NFF Outlines 5 Recommendations to Prepare for Economic Downturn

Contact your local NFF office

Additional Resources

Browse Foundation Center's Focus on the Recession resources for reports, research and fundraising tips.

Stay on top of the latest information on the recession with the Chronicle of Philanthropy's Special Report on the Financial Crisis.

To find out more about the organization that classifies a "recession", read the NBER Recession Dating Procedure FAQ.

Monitor the status of your state's budget with the Center for Budget and Policy Priorities website.

The twelve branches of the Federal Reserve Bank offer information about their regional economies: Atlanta, Boston, Chicago, Cleveland, Dallas, Kansas City, Minneapolis, New York, Philadelphia, Richmond, San Francisco, St. Louis.

Read "Merge Ahead?" in *onPhilanthropy* about nonprofit mergers & alliances as strategies for helping nonprofits survive.