A comparative understanding of the commercialisation of the third sector

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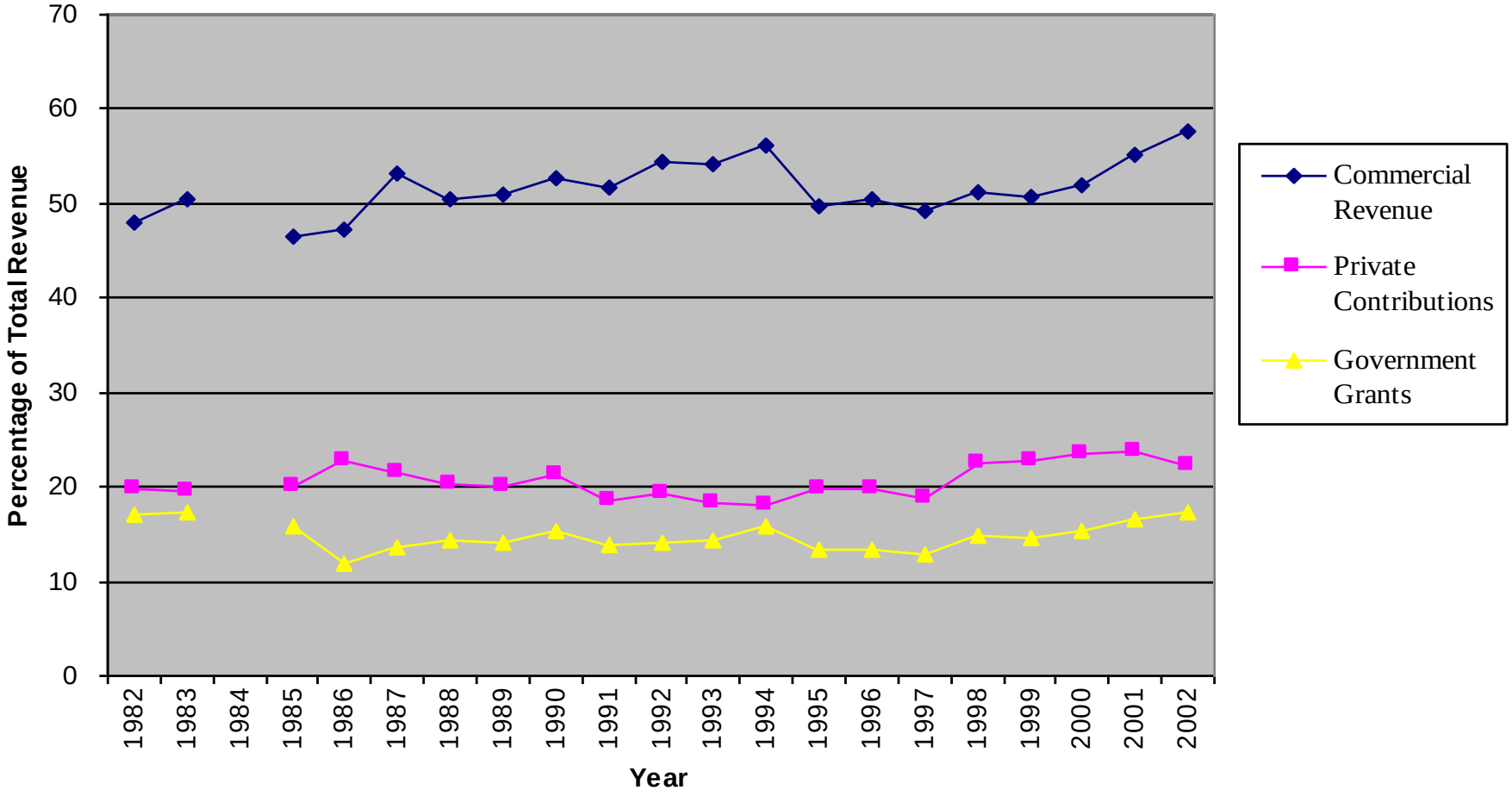
11 April 2013

Perceived wisdom?

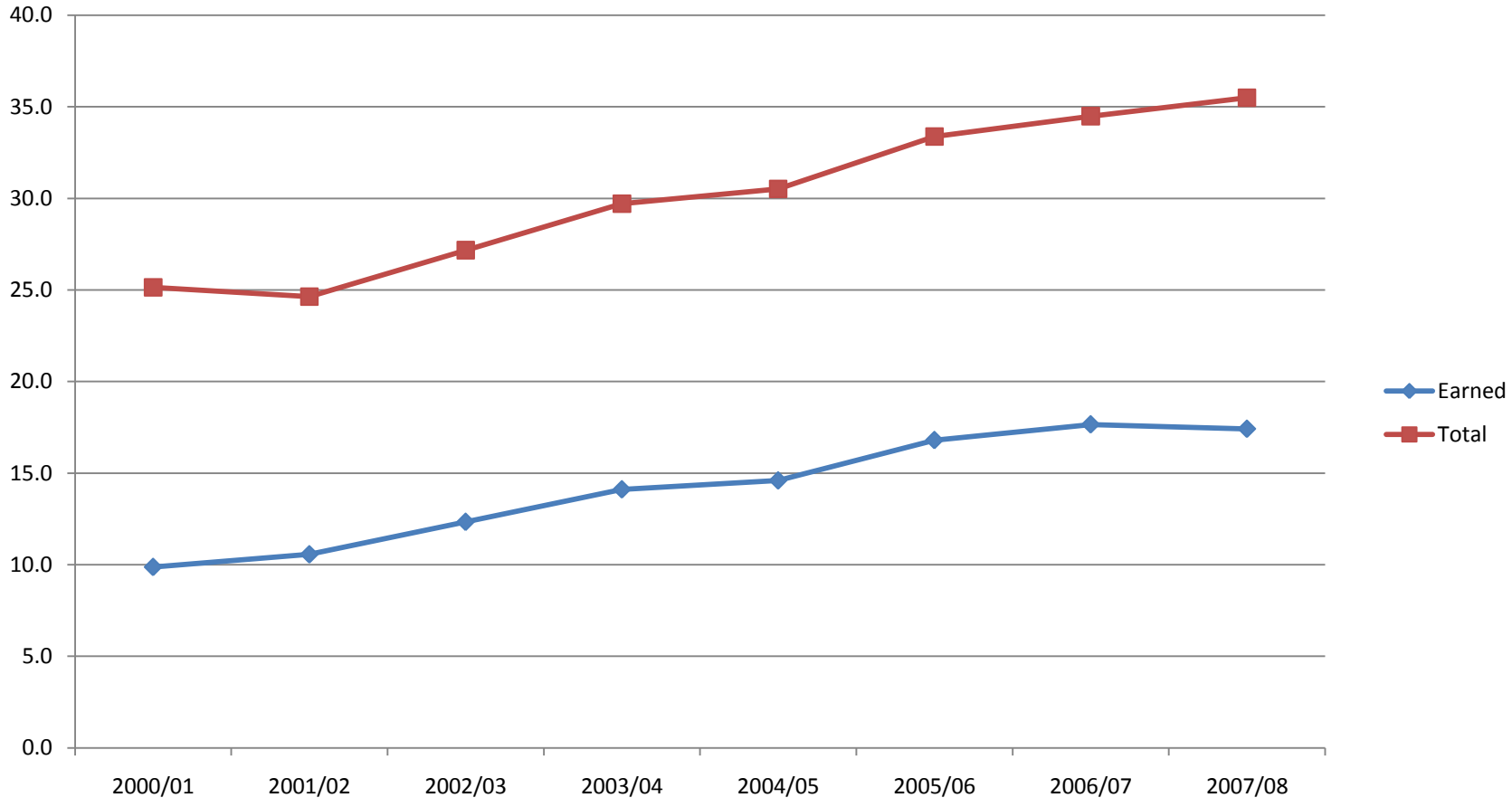
- *"Funding available to nonprofits in the United States has fallen at a time when the range of services they provide has expanded to include those previously delivered by government (Samu & Wymer, 2001). One consequence is that nonprofit organizations are being pushed into adopting a social enterprise model of trading for a social purpose (Zietlow, 2001)."* (Teasdale, 2010: 90)

U.S. Nonprofit Revenue 1982-2002 by Percentage of Total (Kerlin and Pollak, 2010)

(excluding hospitals and higher education institutions)



England and Wales, all general charities, commercial and total income since 2000/01 (£ billions) (derived from NCVO, 2010)



Research question 1

- Consistent with resource dependence theory, at the level of individual charities, is commercial revenue a substitute (replacement) for grants and donations?

Research Question 2

- **RQ2:** How does a change in Commercial Revenue effect Grants and Donations?

- Legitimacy, two perspectives:
  - Crowd out (substitutes)
  - Crowd in (complementary)

Data

England / Wales	United States
80,589 charities	335,936 nonprofits
Data derived from annual returns to the Charity Commission for England and Wales between 2002-2008	Digitized financial data derived from IRS Forms 990 filed by 501(c)(3) public charities between 1995 and 2008
Does not include most smaller charities (Income < £100k); religious organizations	Does not include exempt religious organizations and those with less than $25,000 in annual revenue.
As outliers, Universities, Hospitals and Private Schools were removed	As outliers, Hospitals and Universities were removed
Commercial revenue= activities in furtherance of the charity's objects+ activities for generating funds; trading subsidiaries (gross) + unspecified sales and fees from operating activities	**Commercial revenue** = program revenue + membership dues + special events (gross rev) + sales of inventory (gross profit)

Econometric strategy (England / Wales)

$$\ln(is_{i,t}) = \alpha_0 + \alpha_1 \ln(is_{i,t-1}) + \alpha_2 ln(iv_{i,t}) + \beta' S + \gamma' T + \varepsilon_i + u_{i,t}$$

$$i = 1, \ldots, N; t = 1, \ldots, T$$

Econometric strategy (US)

$$ln(CR_{i,t}) = \delta_{1,t} + \alpha_1 ln(CR_{i,t-1}) + \beta_1 ln(DR_{i,t}) + \beta_2 ln(DR_{i,t-1}) + \theta_1 NTEE + \rho_1 T + \mu_{1i} + \varepsilon_{1i,t} \quad \textbf{(Eq1)}$$

$$ln(DR_{i,t}) = \delta_{2,t} + \gamma_1 ln(DR_{i,t-1}) + \tau_1 ln(CR_{i,t})) + \tau_2 ln(CR_{i,t-1}) + \theta_2 NTEE + \rho_2 T + \mu_{2i} + \varepsilon_{2i,t} \quad \textbf{(Eq2)}$$

Commercial revenue as dependent variable (England/ Wales)

	(1) OLS	(2) Fixed effects	(3) Random effects	(4) GMM-SYS
Ln $(is_{i,t-1})$	0.84	0.08	0.70	0.44
	[0.002]**	[0.043]**	[0.002]**	[0.021]**
Ln $(iv_{i,t})$	0.018	-0.18	-0.01	-0.31
	[0.002]**	[0.036]**	[0.024]	[0.161]*
Constant	1.75	11.62	3.30	9.34
	[0.285]**	[0.061]**	[0.03]**	[1.748]**
S	Yes	No	Yes	No
T	Yes	Yes	Yes	Yes
N Obs	77,624	77,624	77,624	77,624
R-sq	0.73	0.01	0.737	
Within		0.02	0.013	
between		0.07	0.737	
Hansen				6.22
p value				0.044
AR(1)				-19.76
p value				0.000
AR(2)				2.03
p value				0.042

Notes: *= significant at 5%;**=significant at 1%.

Some statistically significant variations by field of activity (England / Wales)

ICNPO Field	Persistence effect	Substitution effect (-)
Social services	0.39*	-0.69*
Law, advocacy and politics	0.30*	-0.56*
International	0.59*	+0.86*
Overall model	0.44**	-0.31*

Notes: *= significant at 5%;**=significant at 1%.

United States: CR as dependent variable

$$ln(CR_{i,t})=\delta_{1,t}+\alpha_1 ln(CR_{i,t-1})+\beta_1 ln(DR_{i,t})+\beta_2 ln(DR_{i,t-1})+\theta_1 NTEE+\rho_1 T+\mu_{1i}+\varepsilon_{1i,t}$$

		GMM-SYS
α_1 :Annual persistence of CR	$ln(CR_{i,t-1})$	0.60
		[0.03]**
$\beta_{1:}$ Short-term crowd-effect		-0.22
		[0. 08]**
β_2		0.11
		[0. 02]**
δ_1		4.42
		[0. 05]**
Longer-term crowd-effect	$(\beta_1+\beta_2)/(1-\alpha_1)$	-0.28
		[0.145]*
NTEE		No
T		Yes
N (Observations)		1,561,545
Hansen		140.30
p value		0.28
Wald test for Granger causality	$(\chi^2_{ce}(2))$	7.57
AR(1)		-10.10**
AR(2)		1.44

Notes: *= significant at 5%;**=significant at 1%.
GMM SYS (Column 4) is derived from a random sample of 1% of nonprofits bootstrapped 10,000 times.

United States: DR as dependent variable

$$ln(DR_{i,t})=\delta_{2,t}+\gamma_1 ln(DR_{i,t-1})+\tau_1 ln(CR_{i,t})+\tau_2 ln(CR_{i,t-1})+\theta_2 NTEE+\rho_2 T+\mu_{2i}+\varepsilon_{2i,t}$$

		GMM-SYS
γ_1 Annual persistence of Dr	$Ln\ (DR_{i,t-1})$	0. 46
		[0. 04]**
τ_1 Short-term crowd-effect	$ln(CR_{i,t})$	-0. 24
		[0. 10]**
τ_2	$ln(CR_{i,t-1})$	0. 15
		[0. 02]**
δ_2		5.87
		[0.06]**
Longer-term crowd-effect	$(\tau_{1+}\ \tau_2)/(1-\gamma_1)$	-0.16
		[0.08]*
NTEE		No
T		Yes
Observations		1,561,545
Hansen		133.57
p value		0.38
Wald test for Granger Causality	$(\chi^2_{ce}(2))$	7.56*
AR(1)		-10.54**
AR(2)		1.84

Notes: *= significant at 5%;**=significant at 1%.
GMM SYS (Column 4) is derived from a random sample of 1% of nonprofits bootstrapped 10,000 times.

Statistically significant variations by field of activity (US)

NTEE field of activity	Longer- term crowd-out effect (-) of DR on CR	Longer-term crowd-out (-) effect of CR on DR
Diseases, Disorders, Medical Disciplines	-0.67** [0.16]	-0.31** [0.08]
Crime, Legal Related	-0.60** [0.18]	-0.18** [0.06]
Health	-0.18 [0.13]	-0.26** [0.08]
Mental Health, Crisis Intervention	-0.27** [0.09]	-0.37** [0.09]

Conclusions

- Commercial revenue is a partial replacement for donative revenue in both countries
- Commercial and donative revenue are interdependent
- Commercial revenue also crowds out donative revenue (only measured in the US)

Making sense of our data

- Resource dependence theory?
- Theories of declining legitimacy?
- Simple micro-economic theories:
  - Much of the commercialization of the third sector in England was driven by state action making commercial revenue relatively ‘cheap’ to obtain. In the US the benign economic period since 2002 has seen grants and donations become ‘cheaper’. Nonprofits react to a change in the price of different revenues and adjust revenue mixes accordingly. They may over adjust in the short term and compensate over a two year period.

Implications

- Future research to understand different trajectories
- Nonprofits considering whether to develop earned income strategies may be encouraged by the relatively high annual persistence of commercial revenue over time. This would appear more stable source than donative revenue, but is lower than has been found in other studies.
- Nonprofits should exercise caution when deciding whether to prioritize commercial revenue over donative revenue (or vice versa). At the level of the individual nonprofit, decisions must be taken with reference to the relative costs of deriving commercial and donative revenues rather than "perceived wisdom"