Downstream & In Demand III

Another Look at Mid-South Nonprofits and the Economic Crisis

Alliance for Nonprofit Excellence

A report from the Alliance for Nonprofit Excellence
November 1, 2011

Executive Summary

Metropolitan Memphis is the poorest large metro area in the nation, according to newly released Census data. More than one in five people (19.1 percent) in the eight-county metro area live below the poverty line, a figure widely acknowledged as underestimating true poverty levels.

Although high poverty is not new to Memphis, the numbers show a steep rise in poverty over the last decade and declining rankings compared to other large metro areas. The new figures show the highest poverty levels concentrated in the city of Memphis, at 26.5 percent, and among local Hispanics and African-Americans, at 38.6 percent and 28.6 percent respectively, compared to 9.6 percent of Caucasian residents.

Unemployment, loss of health insurance benefits, foreclosures, and other effects of the recession have increased pressure on local nonprofits, many of which supply basic goods and critical services to low-income people. Nonprofits are seeing more clients, greater needs, and fewer resources. The recession has brought multiple waves of government funding cuts, reduced grants and gifts, and a corporate sector focused more on its own survival and growth than charitable giving.

Downstream and In Demand III is the third Alliance report on the state of the Mid-South nonprofit sector since the recession began. Although financial analysts say the economy is now on the upswing, nonprofits are far from bouncing back. Charitable giving is still depressed while the cost of doing business continues to rise. Poverty and unemployment patterns are unlikely to shift. Almost three-quarters of this year's 116 survey participants said that service demands increased in FY 2011, and nearly half could not meet these demands. Although the American Recovery and Reinvestment Act (ARRA) helped some nonprofits survive the initial collapse, most of this funding stream is gone. Nonprofits are bracing for another round of cuts as the Federal budget crisis worsens and trickles down to state and local governments.

Downstream and In Demand III is based on a 44-question survey and in-depth interviews with local nonprofit leaders during the summer and fall of 2011. 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. Forty-five percent of respondents have less than one million dollars in annual revenues, 39 percent have between one and ten million dollars in annual revenues, and 16 percent have more than ten million dollars in annual revenues. Almost half of respondents have ten or fewer full-time employees, with 34 percent having between 11 and 50 full-time employees, and 19 percent having more than 50 full-time employees.

We invite you to read ***Downstream and In Demand III*** for a detailed look at the challenges facing Mid-South nonprofits and their strategies for survival. This year's key findings include:

Service Demands

- **Seventy-two** percent of participants experienced increased service demands in FY 2011, up from 71% in FY 2010 and 60% in 2009. Of these, **80%** saw more clients and **58%** reported that clients have greater needs than in previous years.

- **Ninety-six percent** of safety net organizations experienced increased service demands in FY 2011.
- **Forty-three percent** percent of respondents said they could not meet service demands last year, and **63%** of safety net organizations said they could not meet demands for their services.
- **Thirty-four percent** of participants reduced or eliminated programs or services and/or decreased their client numbers or service volume to individual clients in 2011.

Financial Impact

- **Sixty-three percent** of participants said that changes in their operating environments brought additional financial problems this year, and **71%** reported that their cost of doing business increased.
- **Thirty percent** of respondents ended or will end FY 2011 with an operating deficit.
- Small and medium-sized organizations appeared more likely to have a deficit in FY 2011, at **38%** and **34%** respectively, compared to only **9%** of large organizations.
- Approximately **20%** of participants have one month or less of available cash reserves, up from **14%** in FY 2010 and down from **27%** in FY 2009. **Forty-six percent** of respondents have between two and six months of available cash, **22%** have between six months and one year of available cash, and **13%** have at least a year of available cash on hand.
- The most frequently reported financial practices undertaken to financially stabilize participants' organizations included engaging more closely with the Board around financial planning and fundraising, reducing annual expenses, holding conversations with funders about needs, and analyzing programs and business models.
- **Thirty-five percent** of respondents reported that earned income has increased as a proportion of total revenues in FY 2011, up from **25%** in FY 2010. **Nineteen percent** of respondents reported that more than half their budgets come from earned income.
- Less than a quarter of respondents (**24%**) developed a contingency budget in FY 2011, down from **30%** in FY 2010.

Funding Trends

- In FY 2011, **60%** of respondents lost a major funding source and **50%** of respondents received reduced funding from a long-time funding source. The largest funding cuts were from Federal programs and United Way.
- Although corporate giving increased overall, many participants described a decline in corporate donors and sponsors in FY 2011. Respondents reported slight increases in individual donations but not in foundation grants.
- Government contracts continue to pose a challenge for recipients. More than **80%** of participants with government contracts were not fully reimbursed for the cost of services they provide. Low reimbursement levels, late payments, and mid-stream service cuts characterized government funding streams for many recipients.

Protecting the Mission

- Participants were focused on preserving core mission, especially by recruiting and keeping valuable employees, and investing in marketing, technology, and fundraising functions.
- Staff raises and benefits were reported as important for maintaining high-quality staff. Ability to make these investments appeared to be correlated with size. Small organizations less frequently reported giving raises, at **28%** compared to **67%** of medium-sized and **68%** of large organizations. Small organizations also less frequenlty indicated that they hired new positions (**33%** compared to **57%** for medium and **63%** for large) and more often reported having frozen or reduced salaries (**35%** compared to medium at **24%** and large at **21%**).
- Essential recession survival strategies reported by participants included controlling spending, strategic and business planning, and seeking opportunities for partnership and collaborations.

Conclusions

- To meet growing demands and cope with funding cuts, nonprofits must relentlessly analyze programs and how they spend their discretionary dollars. **Nonprofit leaders should always be guided by an understanding of which activities are mission-critical and what they cost.**
- Human resources continue to be most nonprofits' most important asset. **All nonprofit leaders should understand how significant their people are to achieving organizational success and maintain critically needed staff skills.**
- Board members must be more informed than ever if they are to effectively help their organizations survive financial threats. **Board members should expect to play more active roles in fundraising and financial strategy.**
- Few nonprofits have contingency plans or deep reserves. Although cutting costs and raising funds can help manage immediate problems, most are unprepared to handle funding cutbacks and long-term risks. **Nonprofits should be supported with resources to conduct contingency planning. Funders and Board members should consider the importance of unrestricted cash reserves to nonprofit stability.**
- There are few signs that the recession is on the wane in the nonprofit world. Growing poverty and long-term funding cuts mean that nonprofits must work to secure their core missions. **Nonprofit leaders and funders should be persistent in their efforts to build organizational capacity by strengthening staff knowledge and skills, Board participation, financial management systems, fundraising functions, and strategic planning.**
- The landscape for government funding is bleak. Many programs that support area nonprofits are slated to be cut in the next Federal budget. **Public officials in the Mid-South need to help nonprofits defend critical programs from being cut. The nonprofit sector must unite to create and sustain advocacy networks that keep nonprofit issues and needs on the front burner.**
- Most nonprofits are intimately aware of their clients' struggles and their impact on our community. Many outsiders are not. A lack of accessible, useful data hinders public understanding of social problems and nonprofits' roles in addressing them. An important opportunity exists to **research and communicate the social costs of poverty in the Mid-South and the value of the nonprofit safety net.**

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We welcome your questions and feedback on this report:

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I. Introduction

The nation's recession has been declared officially over, but the nonprofit sector has hardly recovered from the downward spiral. Across the country, rising poverty and continued funding cuts continue to put pressure on nonprofits. At the Alliance for Nonprofit Excellence, we hear daily from Mid-South nonprofit leaders about their fight for financial stability, growing client numbers, and struggle to maintain services in the community.

For the third year in a row, the Alliance surveyed area nonprofit leaders to learn how the recession has affected their organizations and the people they serve. ***Downstream and in Demand III***, published in November 2011, paints a picture of nonprofits contending with both familiar and new challenges in the "post-recession recession." For many, recent reductions are another batch of cuts in a long series. For some, Federal and state budget shortfalls brought new reductions, forcing them to cut services or staff. For safety net organizations that provide lifeline health and social services, continued unemployment and financial instability translate to mounting problems for their traditional client populations as well as clients newly struggling with homelessness, physical and mental health issues, and food and household insecurity.

Are conditions for Mid-South nonprofits changing? Not noticeably. Seventy-two percent of survey participants said that service demands increased this year. Forty-three percent reported they could not meet rising demand for services, and 34 percent said they had to cut services or programs in FY 2011. Thirty-two percent had to lay off staff in 2011, and many more had to reduce salaries and benefits, freeze unfilled positions, and double up on job responsibilities. Almost one in three nonprofits ended the year with a deficit and one in five had less than a month of cash in reserve.

Local nonprofit leaders are working harder than ever to balance their mission, capital, and service capacity. ***Downstream and in Demand III*** is a snapshot of local nonprofits' strategies for survival as well as their challenges and hardships. It sheds light on their operating environment and recession strategies, and what they need to keep serving our community. We invite you to share your ideas about what Board members, funders, public officials, and support organizations like the Alliance can do to help.

II. Methodology

Survey

This report represents findings from a 44-question Web-based survey developed and disseminated to Alliance Members via SurveyMonkey in July 2011. Participants were recruited from the Alliance database using the Web, email, and social media. Questions were both multiple choice and open-ended. There were 116 eligible responses. All survey participants were guaranteed anonymity.

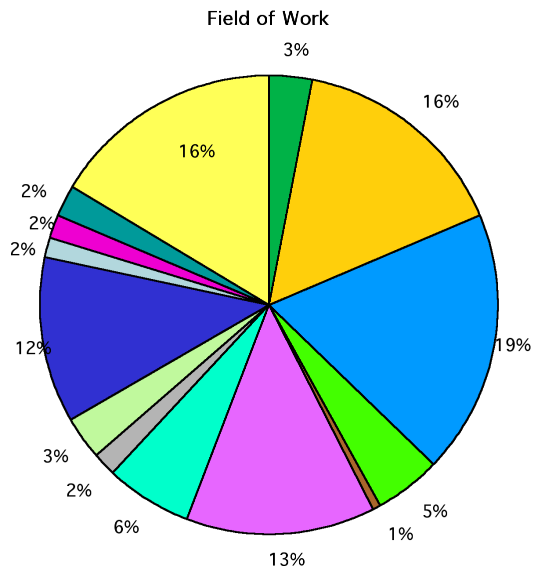
Interviews

In September 2011, interviews were conducted with six local nonprofit leaders, representing diverse organizational size and fields. These included Opera Memphis, the Mid-South Food Bank, East Arkansas Youth Services, Hardin County Regional Health Center, United Housing, and an anonymous multi-service social services agency. Participants were asked six to seven questions about the effects of the economy on their organizations during FY 2011 and how they have addressed recent economic challenges. Key insights from these interviews were included throughout this report as short comments and collected into several organizational profiles.

III. Participant Profiles

Leadership Position

The survey targeted nonprofit leaders in executive management roles in Mid-South organizations. Each organization was represented by a single respondent. **Sixty percent** were executive directors/chief executive officers, **21%** were chief financial officers, **13%** were development directors and **six percent** were deputy directors.



Field of Work

Nonprofit fields most represented in the survey included: children and youth (**19%**), arts and culture (**16%**), education (**13%**), and human services (**12%**). Strongly represented fields also include health (**6%**), disabled services (**5%**), and alcohol and drug treatment (**3%**). Diverse fields such as housing, community organizing, and recreation were also represented.

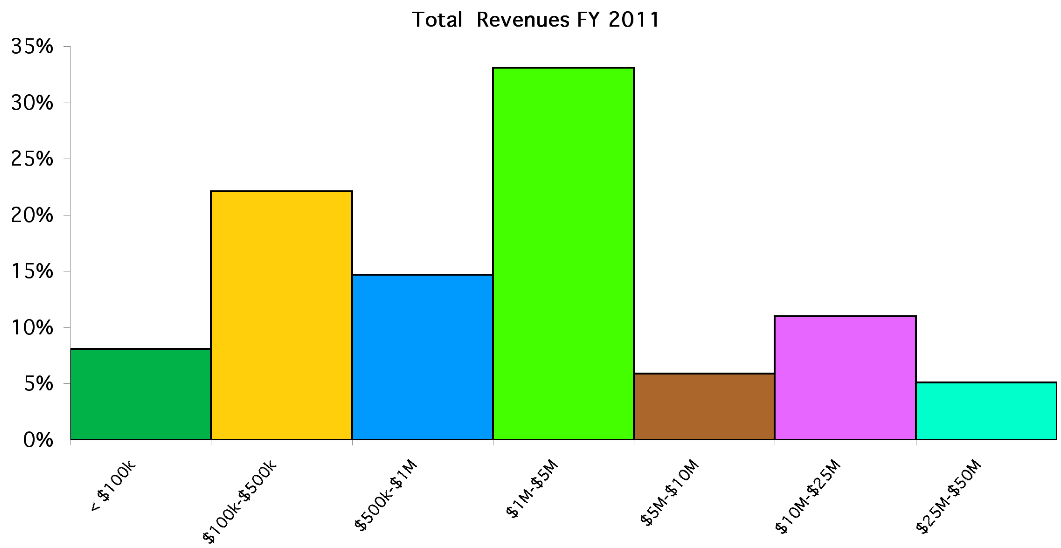
Organizational Size Revenues

Survey respondents were asked to indicate their annual revenues and expenses. Organizations were categorized in this report according to the following:

Small — up to $1 million in annual revenues **(45%)**

Medium-sized — between $1 million and $10 million in annual revenues **(39%)**

Large — more than $10 million in annual revenues **(16%)**



Staff Size

Almost half of survey respondents (**47%**) had ten or fewer full-time employees. **Thirty-four percent** had between 11 and 50 employees, and **19%** had more than 50 employees.

Seventy-seven percent of respondents had fewer than ten part-time staff, **13%** had between 11 and 50 part-time staff, and **ten percent** had more than 50 part-time staff.

Most participants (**82%**) regularly hired fewer than 5 independent contractors per year. Almost **ten percent** used between 10 and 20 independent contractors per year, and **almost nine percent** used more than 30 independent contractors.

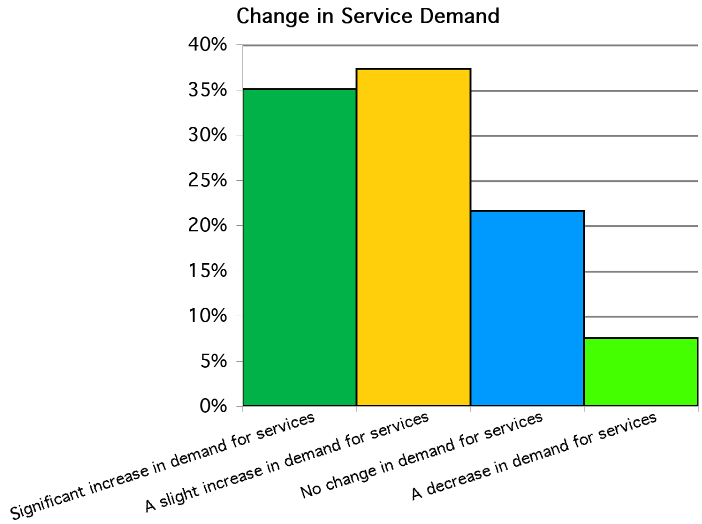
Safety Net Organizations

Twenty-one percent of survey respondents were safety net organizations. These agencies meet critical community needs by serving people who have little or no ability to pay. They include hospitals and neighborhood health centers, homeless shelters, food pantries, and others that provide essential services on an ongoing and emergency basis. They may help recipients access government benefits (e.g., child welfare, food stamps, medical services, etc.) and/or they may generate resources themselves (e.g., by recruiting corporate food donations or using volunteer medical staff.)

IV. Service Demands

Demand Trends

Seventy-two percent of respondents experienced increased service demands in FY 2011, compared to **71%** in FY 2010 and **60%** in FY 2009. **Thirty-five percent** of respondents reported a significant increase in demand for their services in FY 2011, and **37%** saw a slight increase in demand.

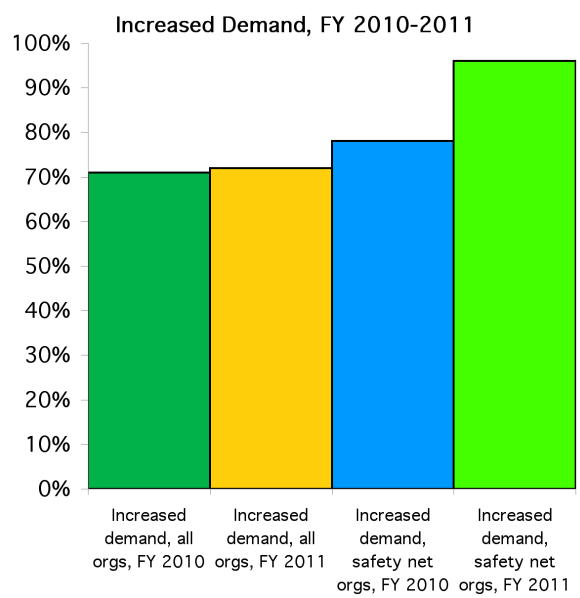


Seventy-three percent of smaller organizations experienced increasing service demands in FY 2011, followed by **71%** of medium-sized organizations and **68%** of large organizations.

Ninety-six percent of safety net organizations experienced increased demand in FY 2011, compared to **72%** of all respondents. This figure reflects an increase from FY 2010, when **78%** of safety net organizations reported increased demand.

Different Kinds of Demand

Increasing service demands come in different forms. **Eighty percent** of respondents reporting increased demand said their organizations saw greater numbers of clients requesting services in FY 2011, up from **62%** in the previous year. More clients frequently meant more administration and overhead costs, more facilities and equipment needs, and more staff.



For others, the spike in demand was less about client volume than the diversity, intensity, and complexity of needed services. **Fifty-eight percent** reported that in the past year existing clients have routinely presented with "additional problems," up from **28%** the previous year.

Many agencies explained that they are seeing new population segments in need of services, including more people struggling to make ends meet despite having full-time employment. Several respondents commented that poverty statistics do not accurately represent the true extent of hardship. Above the poverty line, many people still struggle. According to the Census threshold, only those making less than about $11,000 (or $22,000 for a family of four) are poor. The overly simplistic formula used to calculate poverty doesn't include the effects of factors like taxes, home ownership, health care and child care costs.

Community health providers reported that the newly unemployed and those who lost health insurance represent an increasing proportion of clients living on the edge. One emergency food provider said that need has soared among households that have "doubled up" and people who are now supporting additional family members.

What additional problems are your clients experiencing as a result of the recession?
Job loss
Financial problems
Having to move, housing instability
Transportation issues
Child care needs
Family instability, lack of youth supervision, violence and custody issues
Substance addiction
Co-occuring disorders (e.g., mental health and drug addiction)
Poor health
Sense of desperation
Food insecurity
Homelessness, housing instability

Profile: Recession Can't Keep Up With Food Needs

In 2010, the eight-county Memphis metro area ranked number one in the nation for hunger hardship, according to a 2010 survey by the Food Resource Action Center. More than a quarter of the region's population reports being uncertain about having enough food to eat.

According to Estella Mayhue-Greer, President and CEO of the Mid-South Food Bank (MSFB), food insecurity is high not just in the metro area but in the 31 surrounding counties her organization serves. The agencies through which MSFB distributes food—food pantries, soup kitchens, shelters, and others—have reported that the recession brought rising demands for food assistance, especially from working people who do not qualify for public assistance. Last year MSFB distributed nearly 12.5 million pounds of food, the equivalent of more than 9.6 million meals to local people.

MSFB, like most food banks, has traditionally depended on food donated by large food manufacturers and retail chains. Donated food, along with that distributed through the USDA commodity program, has made up at least a third of the food MSFB collects each year. But in the years since the recession began these donations have been on the wane, with retailers trying to wring profits out of their surplus rather than give it away. Last year, MSFB had to purchase a record 25 percent of the food it distributed, due to a combination of increased demand and shrinking food donations.

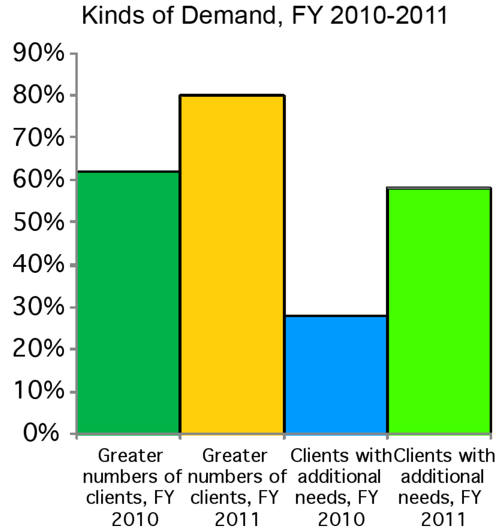
MSFB was able to increase its funding from fiscal year 2009 to 2010, even with faltering program and investment income, primarily by securing additional grants and donations. The steep drop in corporate food donations has taken a toll, although Kroger, Wal-Mart, and Target have recently increased donations. Like many food banks across the country, the agency took a cut in Federal funding under FEMA's Emergency Food and Shelter Program this year.

Mayhue-Greer says that MSFB recently completed its most comprehensive strategic planning process in the organization's history. The five-year plan is aimed at positioning the agency for growth despite tough times, including increased support for grant writing and a commitment to ratchet up fundraising. Hunger and food insecurity are firmly expected to rise in the coming years. With no budget to hire additional fundraising staff, the plan relies on restructuring of current staff responsibilities and more focused fundraising strategies, particularly to identify new foundation funding sources. She also says the agency has been proactive about analyzing its spending and reigning in program costs, not refilling open positions, modifying the agency's health plan coverage, and shopping for better prices on supplies and services.

Service Capacity

For the third consecutive year, survey participants reported not being able to meet increased service demands or making decisions to do so that undermine financial stability (e.g., layoffs, employee benefits, borrowing/credit, and deficit spending.) **Forty-three percent** of respondents said they could not fully meet demand for their services in FY 2011, down only slightly from **44%** last year. **Sixty-three percent** of safety net organizations said they could not meet service demand, down slightly from **65%** in FY 2010.

Ability to meet service demands is slightly correlated with organizational size: **56%** of small organizations, **58%** of medium-sized organizations, and **60%** of large organizations reported being able to meet service demands in FY 2011.



Among those that could not meet their service demands, the most common reasons given were **lack of adequate staff, space,** and **physical resources** (e.g. food, furniture, baby items).

How did nonprofits respond to rising demands?

Thirty-four percent of nonprofits reduced or eliminated programs or services and/or decreased their client numbers or service volume to individual clients in 2011. Medium-sized organizations were least likely to have decreased programs and services or cut clients, at **26%** compared to **36%** of small organizations and **39%** of large organizations.

Fifty-five percent expanded programs and services to serve more clients. Those organizations may have shifted more of their budgets to those programs or raised additional funds. **Fifty-one percent** said they found ways to serve more clients within their current service capacity by restructuring their service delivery methods, cutting costs, or some other means. (These figures add up to more than 100% because some respondents with multiple programs and services reported both service expansion and increasing service volume within current capacity.)

Many survey comments described new partnerships or collaborations

Profile: It's a Domino Effect

The president of one large multi-social service agency in Memphis raised the important point that the well-being of one organization can affect many others in the local safety net. When one nonprofit has to turn away requests for food or housing, people in need turn to another provider. Since the recession, "our ability to serve clients remains stressed," he reports, both because "more people are impacted" and "because other agencies are affected so their clients are turning here." He has seen needs grow across all areas of emergency services — shelter, food, utilities assistance — and says his organization's fundraising has not been able to keep pace with rising demands. "When we turn away clients, they may or may not find somewhere else."

Maintaining programs has meant dipping into reserves this year, but he hopes a new strategic plan and a rebuilt Board will help shore up the organization's finances. A new development director was recently brought on staff and the agency plans to take a more aggressive approach to private fundraising in the coming year, especially as its Federal funding — close to half of annual income — is on the chopping block.

aimed at enabling increased services. **Forty percent** of respondents partnered with another organization to meet rising demands.

Respondents said they are taking steps to prepare for expected additional increases in service demands. **Sixty-nine percent** reported that they expect their organizations to meet demand for their services in FY 2012, up from **44%** that expected to do so in FY 2011. Larger organizations appear to be more challenged to meet demand in FY 2012 than small and medium-sized organizations. Only **53%** of large organizations said they will be able to meet service demands in FY 2012, compared to **70%** of small organizations and **72%** of medium-sized organizations. For FY 2012, respondents said they are most likely to meet expected increases in service demands by expanding programs and services (**55%**), increasing their client numbers (**54%**) and partnering with other organizations to reach more clients (**38%**).

V. Financial Impact

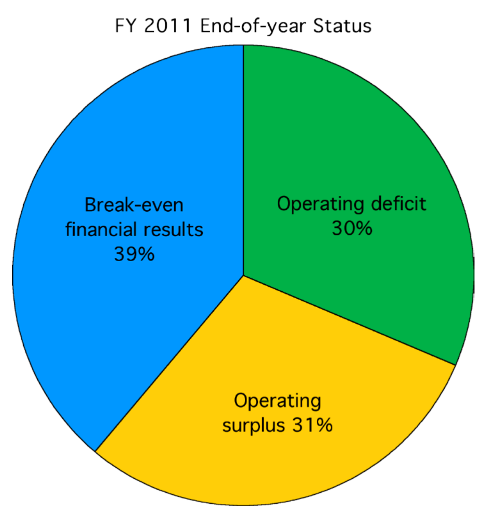
Forty-two percent of respondents said their revenues decreased in FY 2011, up from **35%** in FY 2010 but much lower than the **73%** that reported revenue decreases in FY 2009.

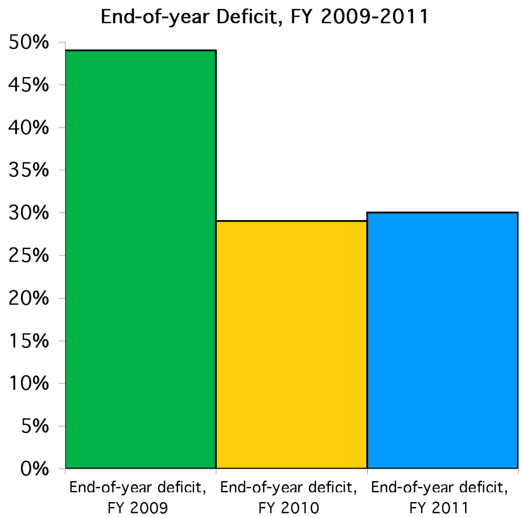
Funding cuts and rising service demands do not happen in a vacuum. **Sixty-three percent** of respondents said that macro-level changes in their operating environments led to additional financial problems. Legislative and regulatory changes related to accreditation, client eligibility, and reimbursement increased costs associated with delivering services. Competition from other providers, especially those vying for government contracts, had an enormous effect on social services agencies, and many reported trying to deliver the same services for less funding than before in order to maintain contracts. Service and product costs also exacerbated financial challenges. **Seventy-one percent** of respondents reported that their cost of doing business rose in FY 2011, citing health insurance and other employee benefits along with food, fuel, and other material goods.

Participants were asked about their financial situation in FY 2011, especially about their financial results, cash reserves, and practices that helped to control costs.

Financial Results

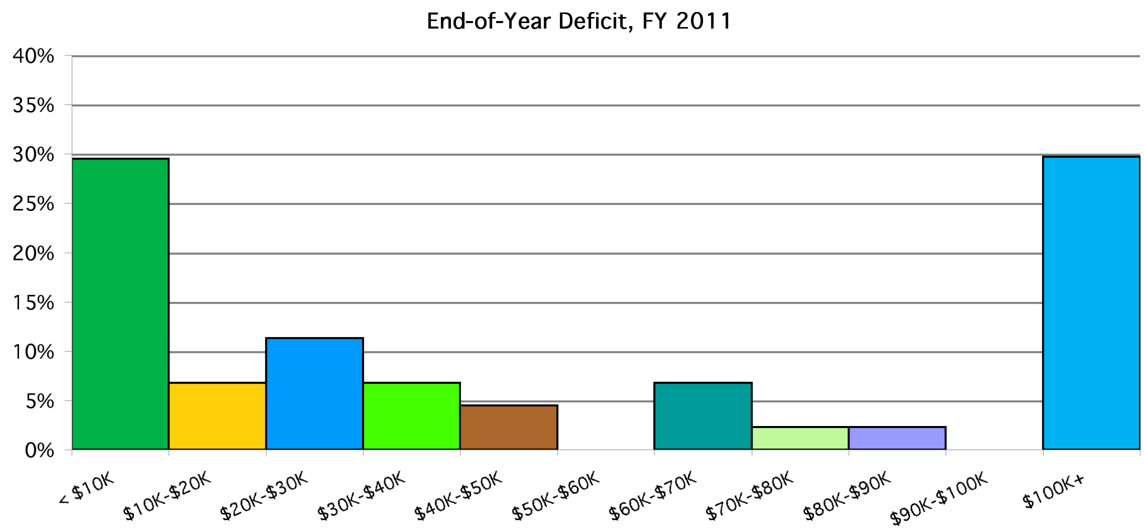
Thirty percent of respondents ended/will end FY 2011 with an operating deficit, up slightly from last year's **29%**. **Thirty-nine percent** of respondents said they finished/will finish the year with break-even financial results and **31%** with a surplus. Last year **24%** of respondents ended the year with a surplus.





Small and medium-sized organizations more frequently reported a deficit in FY 2011, at **38%** and **34%** respectively, compared to only **9%** of large organizations.

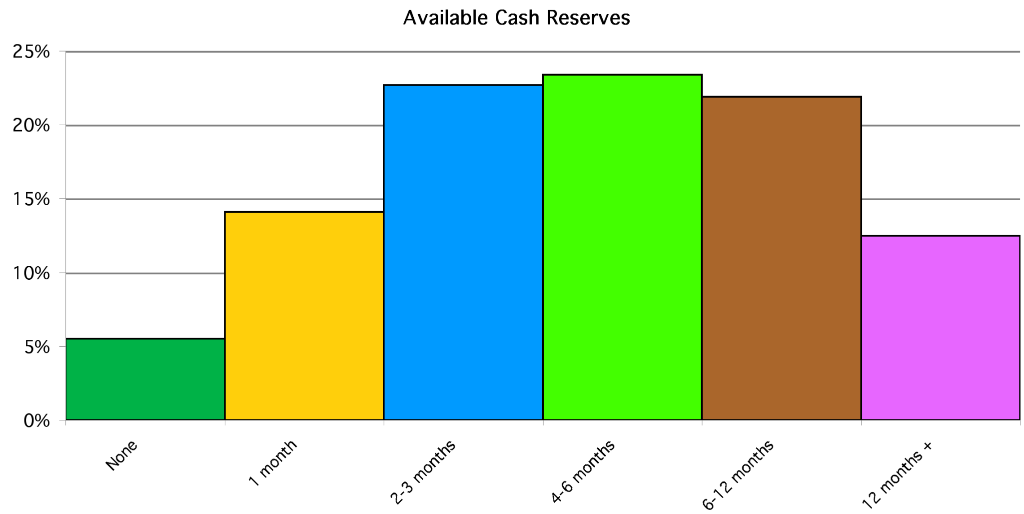
Of the **30%** of respondents that reported they will finish FY 2011 with a deficit, roughly **30%** will end with more than a $100,000 deficit. The number of respondents with a deficit of more than $100,000 increased from **18%** in FY 2010.



Although fewer large organizations reported deficits, their deficit amounts were frequently greater in size. Of those reporting deficits, **75%** of large organizations, **47%** of medium-sized organizations, and **nine percent** of small organizations expected to end FY 2011 with more than a $100,000 deficit.

As several respondents pointed out, end-of-year deficits are not necessarily a sign of instability. Said one, "We started with a Board-approved budget that included a significant deficit, and we will end the year exactly as projected…it was an investment year for us, [with] new programming that offers long-term revenue potential." Another explained, "We hired a new President who recognized that we had to increase fundraising to offset losses in government funding …while [we had to] spend more money in the short term, we have offset those increases and set in place the structure to significantly increase our private and corporate giving."

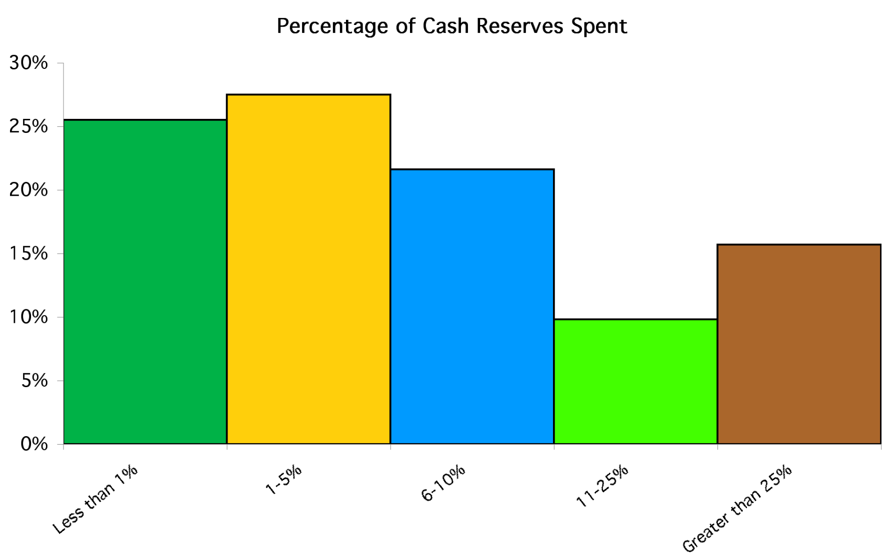
Cash Reserves



All nonprofits need to maintain cash balances that are adequate to support payroll and operations and to prepare for unanticipated shortfalls. According to the Nonprofit Finance Fund, organizations with at least three to six months of cash are better prepared for long-term planning, handling emergencies (major building repairs, loss of a primary funding source, severe economic upheaval), and continuing to provide services in a crisis.

Recommended reserve levels vary. Reserves should be in line with revenue structure—does funding come mostly through contracts, earned income, or grant funds? How risky are revenue sources? How consistent are service levels, and are they cyclical or steady? How could income be affected by changing client needs, competition, or regulation? Despite varying needs, many experts say no nonprofit should be without at least three months of reserves. Participants were asked how much cash their organization currently has available to cover expenses and whether or not they have begun using reserves since the recession began.

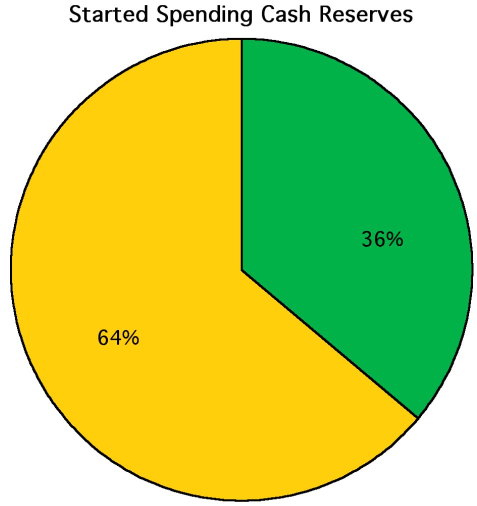
Approximately **20%** had one month or less of available cash, up from **14%** in FY 2010 and down from **27%** in FY 2009. Having less than a month of reserves is considered a cash crisis by most nonprofit finance experts.



Forty-six percent of respondents had between two and six months of available cash, **22%** had between six months and one year of available cash, and **13%** had at least a year of available cash on hand.

Medium-sized organizations appeared likely to have more reserves, with only **13%** reporting less than one month of cash available and **42%** reporting more than six months of cash on hand. **Twenty-six percent** of small organizations **and 21%** of large organizations reported less than one month of cash on hand.

Of those that have reserves, **36%** started spending them down since the recession began.



Practices to Strengthen Finances

Participants were asked which practices their organizations undertook to help maintain or strengthen financial stability in the last year.

Sixty-six percent said that "engaging more closely with [the] Board" to develop effective financial or fundraising strategy was essential to improving financial outcomes in FY 2011.

Thirty-three percent cited "reducing annual expenses" as key to financial performance in FY 2011 and 25% said "analyzing program and/or business model" helped to improve their financial situation. Throughout the survey, respondents described analyzing costs to make reductions in a wide variety of supplies, equipment, and services.

Respondents also named engaging with the Board and holding conversations with funders as top priorities (**67%** and **33%**, respectively) for the coming year, along with raising revenues (**44%**).

Twenty-seven percent said "holding conversations with funders" to explain funding needs and challenges was a critical means of securing more funding or more favorable funding terms that helped improve financial results in FY 2011.

Financial Practices	
Engaged more closely with Board	66%
Reduced annual expenses	33%
Held conversations with funders to explain situation	27%
Analyzed programs and/or business model	25%
Scenario/contingency planning	24%
Collected receivables more quickly	18%
Added to reserve funds	16%
Collaborated with another organization on expense	11%
Reduced occupancy costs	10%
Expanded office space	9%
Sold assets such as a building or securities	3%
Merged with another organization	1%

Contingency Planning

Respondents we asked if their organizations have conducted contingency or scenario planning. Contingency plans help nonprofits avoid operating and making decisions in crisis mode. Well-defined contingency plans describe where and how to cut spending should large budget cuts occur and identify factors that determine when to enact the plan.

Less than a quarter of respondents (**24%**) developed a contingency budget in FY 2011, down from **30%** in FY 2010. Large organizations more frequently reported that they had conducted contingency/scenario planning at **10%** compared to **26%** of small and **26%** of medium-sized organizations.

Profile: Federal Funding Cuts Threaten Safety Net Health Centers

In the spring of 2011, Federal budget cuts reduced funding for the Community Health Centers (CHC) program by 600 million dollars. Providing primary health care in the nation's low-income communities, health centers are critical safety net providers for uninsured and underinsured Americans. Although expanding the network of CHCs had been a cornerstone of health reform legislation passed less than a year before, the cuts would result in a shortage of care to more than five million people.

Hardin County Regional Health Center (HCRHC) was among those that saw funding dwindle when the recession hit, after several years of growth and expansion to meet growing demands. Based in Savannah, TN, HCRHC provides primary and preventive care to more than 13,000 patients each year.

HCRHC had received $650K from HRSA for a New Access Point grant to support an additional provider site in the region. But in 2009, the agency had to put its capital expansion plans on hold due to the uncertainty of that funding's continuation. Short-term ARRA funding helped to bridge the gap for ongoing operations, but wouldn't provide a long-term solution to the lack of Federal funding and rising demands.

According to director Janie McGinley, CEO of HCRCH, funding shortages have meant turning more people away without care. The center can not hire two additional providers needed to meet current needs, which have increased as the economy worsened. Sick patients wait longer to come in for care, says McGinley, so their conditions are more advanced. Changes in health insurance structure mean more patients have high deductibles before co-pays kick in, and the center's uninsured population has risen an additional five percent of patients.

The Federal budget deal relied on funding from the Affordable Care Act (ACA) to backfill the cuts to health centers. ACA established a Health Center Fund that would have put the program on track to serve 40 million patients by 2015, but instead the expansion funding was redirected toward maintaining existing operations. The cuts came after nearly 800 communities across the country submitted applications to start new health centers, and almost every health center had submitted plans to increase service volume.

Despite putting expansion plans on hold, omitting raises, and not hiring needed additional providers, HCRCH has managed to take steps to address critical needs, adding an addiction treatment program and an additional behavioral health provider. New teleheath programming—a growing necessity in rural areas—is helping the agency to reach more people with fewer resources. Although they require additional time and expense, electronic health records may eventually help streamline operations. And the tough job climate has an up side, says McGinley—a wave of better-educated, better-qualified job applicants for administrative and support positions.

HCRCH received some funding for training and TA from the Tennessee Primary Care Association, and just won a supplemental HRSA grant to support care planning, service delivery improvement, and system upgrades. However, McGinley reports, the future is uncertain, with health centers watching the Federal budget closely. At the national level, a health center mobilization effort is developing to urge Congress not to undermine health center capacity in the Federal agenda. Congress is considering more cuts to discretionary programs as well as changes to the Medicaid program that may result in payment cuts to health centers for Medicaid services for patients. The cuts would further weaken the health center safety net at a time when 60 million Americans lack access to affordable health care, forcing them to turn to costlier, last-resort services at emergency rooms or to forego health care entirely.

VI. Funding

Respondents were asked to identify what funding they were most likely to seek and receive. Top responses included programs (**80%**), facilities (**62%**), and working capital (**44%**).

Layoffs

Layoffs were a recurring cost-cutting theme again this year. Thirty-two percent of respondents reported layoffs, the same as in FY 2010. "It was a catch-22," reported one leader of a rural nonprofit, "our staff is what generates our income, but we couldn't afford to keep them." Respondents also reported cutting hours, reducing pay and benefits, and shifting to more part-time workers and/or a greater percentage of lower-paid, less-skilled employees.

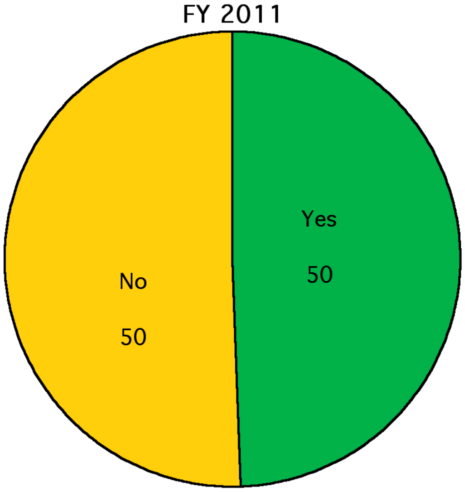
Funding Trends

In FY 2011, **60%** of respondents lost a major funding source and **50%** of respondents said that funding from a long-time funding source was reduced.

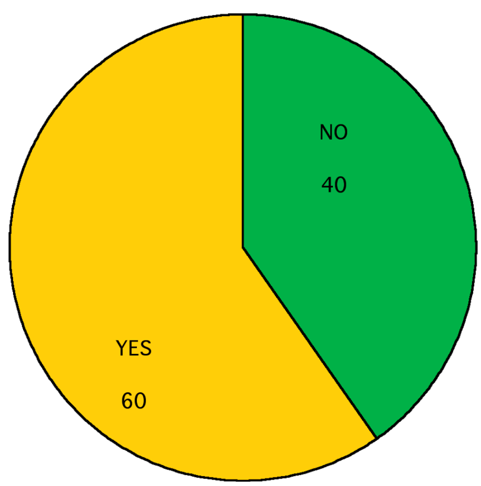
Support Requested and Received, FY 2011

Funding Need	Support Requested	Support Received
Program expansion	80%	66%
Facility needs	62%	53%
Working capital needs	44%	37%
Operating reserves	31%	22%
Cash flow concerns	26%	19%
Debt burden	15%	7%
Building reserves	10%	6%

Reduced Funding From Long-time Funding Source, FY 2011



Lost Funding Source in FY 2011



The largest funding cuts were from Federal programs (CDBG, FEMA, SAMHSA, Corporation for National Service, etc.) and United Way. Respondents also reported severe cuts in funding from the state of Tennessee. Although corporate giving increased overall, many participants described a decline in corporate donors and sponsors in FY 2011. Respondents reported slight increases in individual donations but not in foundation grants.

Changes in Funding Level by Type of Funder, FY 2010-2011

Profile: Housing Agency Uses Strategic Allocation of Funding to Rebuild Mid-South Neighborhoods

Distressed loans, vacant homes, deteriorated neighborhoods…nowhere has the recession left a more visible mark than on housing. The mortgage meltdown took a dramatic toll on low- and middle-income households across the country, leaving more people than ever unable to afford homes. Memphis has consistently ranked at the top of nationwide foreclosure statistics, particularly in areas like Frayser and Raleigh that faced the brunt of predatory lending and declining home values.

Memphis-based United Housing, Inc. was among the recipients of a Neighborhood Stabilization Program (NSP) grant, a Recovery Act initiative designed to help communities suffering the worst foreclosures and abandonment. With the five million dollars received for purchase and redevelopment of foreclosed and abandoned homes, United Housing has taken major steps to reverse local housing decline. According to Executive Director Tim Bolding, NSP brought a critical infusion of cash to address the housing crisis in the Mid-South. The agency has greatly expanded its acquisitions and sales with the funds, which were further enhanced by $1.2 million in funds from the Tennessee Housing Development Agency (THDA).

Sinking housing values continue to affect the market, says Bolding, describing "a continuing flood of empty properties" in the Mid-South. The agency's clustering strategy is aimed at increasing home values on a broader scale by improving whole blocks and sections of neighborhoods, especially those like Skylake in Frayser, and Scenic Hills in Raleigh, which Bolding says were "solid neighborhoods in the seventies…they're attractive and coming back."

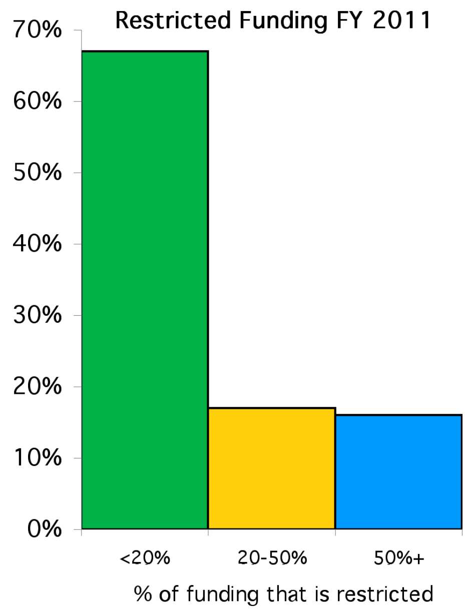
Aside from low home values, Bolding says the biggest challenge brought on by the credit crunch is that banks are leery about lending to low-income homebuyers. United Housing has taken an aggressive approach to communicating the value of its properties and convincing lenders of clients' potential. United Housing also makes a point of developing and maintaining relationships with realtors, even arranging for bus tours of available properties.

Bolding is always thinking about the best way to stretch resources, and does not hesitate to communicate with funders about what the organization needs to accomplish its goals. He recently asked the state for permission to transfer 600 thousand dollars in foreclosure funds into construction expenses to support a 113-acre, 30-home subdivision in Frayser. The plan was in the first stage of development when the market crashed a few years ago. When the state approved the transfer, he approached several local foundations to match the funds, two of which committed two hundred thousand dollars each to the project.

Another wave of foreclosures is coming, says Bolding. He expects the environment to get worse as unemployment continues, those leaving town for jobs are forced to sell by short sale, and newly delinquent homeowners move into default. It's a climate that doesn't bode well for trying to raise property values, increase homeownership, and stabilize neighborhoods.

The influx of government funding changed United Housing's revenue structure dramatically, but Bolding describes it as a temporary boom. The agency had its most successful year ever last year, closing 32 Memphis-area homes. Since July of 2011, it has sold ten properties and Bolding says he expects to hit 40 by the end of the year. But "there won't be anything else coming out," he says, "We'll need to recycle, and be conservative to carry [proceeds from sales for reinvestment] through for a while. Our goal is to look at the money, go into deals conservatively, space out subsidy, and think long-term."

In FY 2012, more than half of respondents expect corporate funding and individual donations to increase. **Forty-two percent** expect foundation funding to increase and only **5%** expect United Way funding to increase. Only **14%** expect government funding to increase in the coming year; **51%** expect it to decrease.



Restricted Funds

Restricted funds come with stipulations on how they can be used. Many funders give money only for specific programs or projects and do not support operating expenses or allow recipients to reallocate these funds. From an accountability standpoint, restricted funds help funders feel more confident that their investments result in the promised outcomes. However, restricted funds can also hinder nonprofits from making strategic changes to respond to challenges and opportunities as they arise. A high proportion of restricted funds can mean that a nonprofit's cash flow is even bleaker than it looks, because those funds are obligated for specific purposes. Many nonprofit experts are critical of program-restricted funding, believing that it stifles adaptability, especially in turbulent times.

Sixteen percent of respondents said that more than half their funding was restricted and **17%** said that between **20%** and **50%** of their funding was restricted.

Medium-sized organizations reported the lowest proportion of restricted funding, with only **11%** reporting that more than **50%** of their funding was restricted, compared to **19%** of small and **23%** of large organizations.

Profile: State Funding Cuts Cost Foster Services

When the state of Arkansas cut funding for foster care/delinquent/at-risk youth services in 2011, East Arkansas Youth Services (EAYS) had to reduce its beds by more than half. The cuts meant a $240,000 funding loss for EAYS, more than 17 percent of the agency's annual budget.

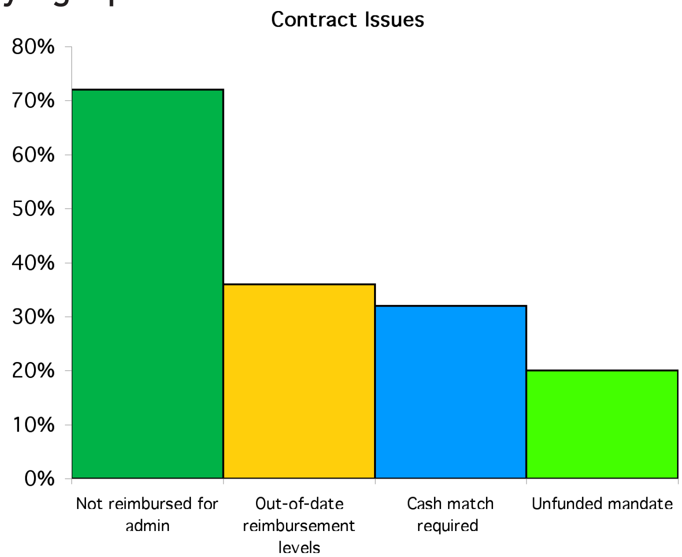
EAYS provides positive alternatives to institutionalization for youth who are involved or at risk of becoming involved with the juvenile justice system. The agency is largely dependent on its state contract to delivery comprehensive community-based services, which include foster care, residential treatment, and case management in its seven-county service area. The loss in state funds was partly due to reduced support from the Federal Social Services Block Grant.

The revised state contract would have required EAYS to maintain service levels at twenty dollars less per client on a daily basis, a formula that simply wasn't feasible. Two rounds of ARRA funding were also problematic because they required new programs to be implemented without long-term support. The increased cost of doing business challenged the organization's resources, leading to reduced residential capacity (eight beds) and staff cuts (six full-time and five part-time positions). Layoffs also meant reduced non-residential services and cuts to the agency's GED preparation program.

According to EAYS' Executive Director Madelyn Keith, the agency is looking to other potential funding sources. She is hopeful that Medicaid funding may soon be available and that EAYS can successfully compete for substance abuse funding to meet the growing need for drug prevention and treatment services among its clientele. In the meantime, she says, EAYS is hoping to catch up with growing demand by revisiting EAYS' strategic plan, restructuring job assignments, and developing partnerships with other community providers.

Contract Issues

Forty-five percent of respondents received Federal contracts, **46%** received state contracts, and **38%** received city and/or county contracts. **Thirty-eight percent** received contracts from all three sources.

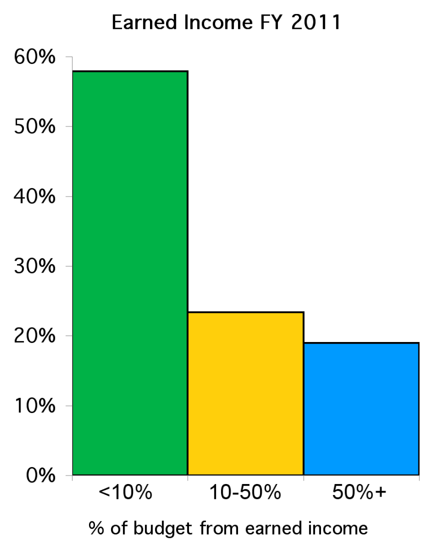


How does the administration of government contracts affect nonprofits?

More than **80%** of participants with government contracts were not fully reimbursed for the cost of services they provide. Of these, **72%** said that their administrative costs were not reimbursed, **36%** said reimbursement levels were out-of-date, **32%** said that a cash match was required for their contract fee, and **20%** said they were required by law to perform services without funding (unfunded mandates).

Other observations about government funding relate to reporting requirements and late payments. Many respondents reported their cash flow has been negatively affected by late payments. Several said that budget crises have led to uncertainty about whether current services will eventually be reimbursed. Others reported that their contracting agencies changed terms mid-stream, leading to unplanned service cuts or operating in the red.

Earned Income



Earned income includes revenues generated from programs, services, products, and membership fees. For nonprofits that provide fee-based programs or services, the recession has hit hard by way of their customers' spending. Performing arts agencies that depend on ticket sales and subscriptions saw huge dips in attendance, as did museums and many recreational programs. Membership and training organizations and those that rely on sales of merchandise also saw their incomes plummet.

On the other hand, earned income is one domain in which some nonprofits have countered financial problems. Many respondents described changing their revenue models this year to increase earned income, including adding or changing fee-based services and products, fee structures, and customer targets.

Thirty-five percent of respondents reported that earned income increased as a proportion of total revenues in FY 2011, up from **25%** in FY 2010. **Nineteen percent** of respondents reported that more than half their budgets came from earned income.

Smaller organizations appeared less likely to derive a large portion of their budget from earned income. Only **11%** of small organizations reported more than **50%** of their budget came from earned income, compared to **21%** of medium-sized organizations and **36%** of large organizations.

Profile: Opera Company Scores Success by Playing to the Crowd

Listening to what your audience wants is essential to staying resilient in tough times, says Ned Canty, General Director of Opera Memphis. When the recession hit and revenues plummeted a few years ago, the company responded by making bold, well-informed changes to its operating model. The organization's leaders decided to expand and restructure its performance calendar in an effort to boost flagging ticket sales, says Canty, but at the time it was not clear what these changes meant to its audience.

The changes did not draw the crowds as hoped, and even with a heavier performance schedule, the company's earned income continued to flag. Last year, Opera Memphis leaders decided to "re-connect with what audiences want," and take a deeper look at their stakeholders' values, both those of diehard followers and potential new fans. After analyzing attendance data and surveying audience members, the company has now returned to its old model of fewer performances. Strategic change and innovation must respond to stakeholders' needs and desires, Canty says, especially in an art form with such a passionate core following.

One of opera companies' inherent financial challenges is the cost of production relative to the size of its audience. Opera companies across the country thrived in the nineties, with healthy subscription bases, wealthy donors, and high-profile corporate sponsorships. In the early 2000s, sales started to drop off, a trend some attribute to baby boomers beginning to retire and spend less on entertainment. As for newer, younger audiences, some observers say they aren't filling their parents' seats, perhaps because of declining arts education and/or a disinclination to commit to long-term subscriptions, long a part of operas' standard business model.

When the current recession hit, the trouble compounded. Not only did opera subscriptions and ticket sales take a hit but also wealthy donors and corporate sponsors dramatically cut their support. Reduced cash flow and revenue streams led many opera companies across the country to cut performances, suspend seasons, even file for bankruptcy. While managing to continue operations, Opera Memphis was hit hard by the double loss of ticket sales and longstanding corporate sponsorship.

According to Canty, attendance has now begun to rebound as a result of the organization's rigorous assessment of audience interests. Not all communities can support a professional opera company and the number that can is rapidly shrinking. The Mid-South is home to a generous, enthusiastic opera community, he says. Survival means creating a unique model that is adapted to that community, and making decisions about repertory, performance schedule, and income models that reflect its values.

Although the future is uncertain, Canty believes the recession is a temporary setback and an opportunity to grow and learn. Economies are cyclical, he says, and staying artistically productive and financially stable means not feeding on negativity and futile predictions. In the next year, Opera Memphis will continue to look for ways to recharge ticket sales, work to maintain public dollars, and take a proactive approach to private fundraising. On the program for the coming year: articulating a clear case to potential corporate donors, developing new followers through outreach and education, and staying ever in tune with the company's core audience.

VII. Protecting Mission

This year's study suggests a growing sense among nonprofit leaders that funding cuts and rising demands are long-term conditions. "We're not shocked anymore," said one nonprofit leader, "nothing would surprise us." Although there are some signs that foundation funders are recovering from the meltdown, the outlook for government funding in many sectors is dismal and individual giving is rebounding slowly. The social problems that worsened with the economy are entrenched and unlikely to lessen any time soon. For nonprofits, being downstream and in (too much) demand is now business as usual. "At this point," said one participant whose safety net organization has lost critical government funding and drastically reduced staff and services, "it's just how things are. I'm tired of talking about it."

Recession Management Strategies	
Gave raises	50%
Hired staff for new positions	48%
Made replacement hires	47%
Changed marketing approach	38%
Invested more in technology	33%
Reduced staff	32%
Retained all current personnel	32%
Relied more on volunteers	29%
Froze or reduced salaries	28%
Reduced staff benefits	13%
Froze all replacement hires	12%
Improved or increased staff benefits	11%
Reduced staff hours	11%

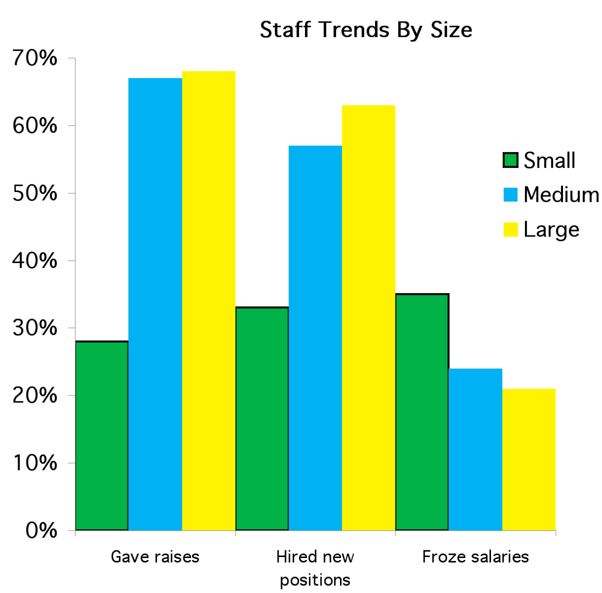
As the effects of the recession wear on, nonprofit leaders appear to be taking a longer view. "A few years back we had to respond by putting out fires, cutting everything, and everyone," said one leader. "Now, we're looking at a bigger picture. We need the plan, the systems, and the people. We're still looking to cut costs, but we've shifted more to an investment mindset, whether it's stepping up fundraising or finding partners or changing how we communicate with those we serve."

Participants were asked what strategies were helping them protect their core operations and mission. Most nonprofit leaders reported thinking critically about which services and programs are most vital to their mission and how to best focus resources on these programs. Participants indicated they are working to understand the full costs of their programs in order to scale back on some and free up resources for others. Said one participant, "We're now clear about exactly where our discretionary dollars are going. It took a while for the Board to get it, and we had to just keep hammering down on the same thing: what are we trying to achieve and how do we do that?"

This year several strong themes emerged related to how nonprofits are managing for mission:

Staff Investments

Many respondents reported taking steps to hire and keep talented employees, saying it was a critical step to achieving their missions. Asked which management-related actions they've taken in the last 12 months to strengthen their organizations, participants most frequently responded "gave raises" (**50%**), "hired staff for new positions" (**48%**), and "made replacement hires to fill vacant positions" (**47%**).



Ability to make these investments appeared to be correlated with size. Small organizations less frequently reported giving raises, at **28%** compared to **67%** of medium-sized and **68%** of large organizations. Small organizations also less frequenlty indicated that they hired new positions (**33%** compared to **57%** for medium and **63%** for large) and more often reported having frozen or reduced salaries (**35%** compared to medium at **24%** and large at **21%**).

A large number of respondents credited their success to staff commitment to what was sometimes difficult change—accepting new responsibilities, cutting costs, and program and organizational restructuring. Many variations on "working more lean" were described, including streamlining and sharing staff responsibilities, "working with outside volunteers that are business professionals," and "cross-training of staff to assume more responsibility."

Marketing and Technology

This year respondents also described greater investments in marketing and technology. **Thirty-eight percent** of respondents changed their approach to marketing and communications during the last year in order to adapt to changing economic conditions. Many described new marketing campaigns and/or new or restructured marketing positions and departments. Several agencies moved their marketing activities in-house this year after using contractors in the past. Others increased their investment in social media and expanded online communications, especially to drive individual donations and event attendance. Several respondents reported that declining donations and memberships led them to develop communications plans to set goals and outline strategies for the coming year. **Fifty-six percent** of those that changed their approach to marketing and communications said their organizations experienced revenue increases as a direct result.

Thirty-three percent of respondents reported making major technology investments to increase their effectiveness this year. Of these, **36%** said their investments have already paid off. Investments in practice management systems and other service delivery systems were reported as highly valuable. Other frequently described technology investments included: e-commerce, online fundraising, accounting and billing software, and basic computing equipment for staff.

Managing Change

Participants were asked what management steps and strategies they were most proud of in FY 2011. An overwhelming majority described financial strategies that enabled their organizations to maintain their core mission and service delivery.

Many respondents described important steps taken to control their spending:

> *"We have funds left over to make needed facilities repairs."*
> *"We reduced handling fees so more needy people could be served."*
> *"We have tightened our procedures, especially on a fiscal level, in order to have better checks and balances."*
> *"Cut expenses when revenue projections did not materialize."*
> *"Reducing expenses and increasing productivity allowed for building strong reserve funds without dramatically affecting patient access."*

Some described organizational processes designed to stabilize their finances and steer growth:

> *"Through our strategic planning process we eliminated one program that no longer fit our mission, reduced staff, and tightened our expenses."*
> *"Comprehensive strategic and business planning to develop a new business model."*
> *"We formed a Finance & Audit Committee - it has greatly helped with the fiscal planning of the organization."*
> *"Hiring a consultant to help us analyze programs and restructure."*

Others described fundraising investments and strategies:

> *"Our Board endorsed a significant expansion of our fundraising efforts [for] capital expansion and [to grow] our endowment."*
> *"We broke into nontraditional sources of funding for the arts by demonstrating [links to youth development and education.]"*
> *"Communicating our mission more effectively to donors has made a difference for us this year."*
> *"We recruited more philanthropic Board members."*
> *"We realized we could reach more potential donors with more effective messages, but we had to dedicate staff time and build expertise in this area. "*

Some mentioned forging new partnerships and collaborations:

> *"We entered into a MOU with a nonprofit…that offers complimentary services [and expertise]…We expand our mission; they survive and gain a program with proven sustainability…it will expand our capabilities and strengthen our outcomes. I am the most proud of the way each organization views intellectual property: anything that offers a social return on investment and improves client outcomes should be shared without territorial or proprietary concern. In the end, we each see elements of our individual missions carried out by the other in a new market without additional capital expense; or duplication or dilution of services. It's "virtual expansion" through collaboration and sharing."*

VIII. Conclusions/Moving Forward

This year's study shows few substantial improvements in the local nonprofit landscape. Continued funding cuts and growing service demands brought unprecedented challenges, even for those organizations used to doing a lot with very little. Nonprofit leaders continue to be faced with tough choices and growing uncertainty. The findings provide a look at how organizations are faring and what they are doing to manage successfully. We hope this information is useful to nonprofit leaders and to funders, donors, and public officials that can help. In closing, we offer a few observations for both leaders and supporters:

To meet growing demands and cope with funding cuts, nonprofits must relentlessly analyze programs and how they spend their discretionary dollars. **Nonprofit leaders should always be guided by an understanding of which activities are mission-critical and what they cost.**

Human resources continue to be most nonprofits' most important asset. **All nonprofit leaders should know how significant their people are to achieving organizational success and maintain critically needed staff skills.**

Board members must be more informed than ever if they are to effectively help their organizations survive financial threats. **Board members should expect to play more active roles in fundraising and financial strategy.**

Few nonprofits have contingency plans or deep reserves. Although cutting costs and raising funds can help manage immediate problems, most are unprepared to handle funding cutbacks and long-term risks. **Nonprofits should be supported with resources to conduct contingency planning. Funders and Board members should consider the importance of unrestricted cash reserves to nonprofit stability.**

There are few signs that the recession is on the wane in the nonprofit world. Growing poverty and long-term funding cuts mean that nonprofits must work to secure their core missions. **Nonprofit leaders and funders should be persistent in their efforts to build organizational capacity by strengthening staff knowledge and skills, Board participation, financial management systems, fundraising functions, and strategic planning.**

The landscape for government funding is bleak. Many programs that support area nonprofits are slated to be cut in the next Federal budget. **Public officials in the Mid-South need to help nonprofits defend critical programs from being cut. The nonprofit sector must unite to create and sustain advocacy networks that keep nonprofit issues and needs on the front burner.**

Most nonprofits are intimately aware of their clients' struggles and their impact on our community. Many outsiders are not. A lack of accessible, useful data hinders public understanding of social problems and nonprofits roles in addressing them. An important opportunity exists to **research and communicate the social costs of poverty in the Mid-South and the value of the nonprofit safety net.**

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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