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## **The Third Sector and the Financial Crisis: Can we do more with less?**

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**Abstract of the Hebrew report**

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Following the financial crisis which began in 2008, changes took place in the working environment of Nonprofit Organizations. To examine how the organizations dealt with the drop in income on the one hand, and the growth in service demand triggered by the crisis on the other hand, ICTR performed a two-phase study of the sector's organizations response to the crisis. The first phase, at the beginning of the crisis in 2009, investigated the organizations response to the funding uncertainty and the impact of the crisis on their stability and capacity. As the crisis continued to unfold, we followed up with a second survey to examine how it is influencing the organizations in Israel.

The situation in many countries was similar to that of Israel: third sector organizations saw demand for services rise, especially for social services but also services in health and education, as their revenues declined due to the decreasing funding from private donors and the public sector. This is what was found, for example, in a report published by the National Council of Nonprofits in the US in 2009. The report shows that more than a third of the organizations experienced cuts to their budget. They also show that the cutback in government support was more problematic than the decline of income from private donors and foundations. The report estimated that nonprofits will continue to feel a double pressure of growing demand for services along with a decline in income. Similarly, the Center for Civil Society Studies at Johns Hopkins University (Salamon, Geller and Spence, 2009), found that 83% of the organizations in their Listening Posts project are under severe economic pressure. Approximately 40% of them described the difficulties as being severe.

Passive response In an international symposium held in the Center for Social Investment at Heidelberg University, findings from various countries converged to show similar responses by nonprofit organizations: Mostly responses were reactive and passive in nature - reduction of wages, freezing of wages and dismissal of workers, shutting down existing programs, delaying the beginning of new programs, and the reduction or cancellation of services. Many organizations relied on financial reserves, or went into debt. Often the decision making was characterized by a “trash can effect”: the crisis seems like the ultimate chance – not to innovate, but to get rid of programs and team members which are not effective or are not required anymore. Some of the actions taken were more proactive, such as adding volunteers to make up for the reduction in paid workers, attempting to diversify funding sources and entrepreneurship. In Israel and Iceland a growth in advocacy activity was noted, in Los Angeles and Ireland increased cooperation between organizations was reported.

### **The effect of the crisis on Israeli Non Profit organizations**

In Israel the economic crisis brought about a reduction of government funding and a decline in income from philanthropy. Due to the downturn experienced by Israeli businesses, many decided to stop altogether or dramatically reduce corporate giving. Giving from Jewish Federations was hurt by a decline in local giving and increased local spending on Jewish community needs. The Madoff scam caused various Jewish Foundations to disappear or to severely reduce giving. Findings of our first survey showed that soon after the beginning of the crisis 81% of the organizations experienced financial difficulties, 51% reported a worsening in their financial situation during 2008, of them 12% had a severe decline in income. At the same time, over half of the organizations reported a rise in expenditure, and 15% had simultaneously both a cut in income and a growth in expenditure, resulting in severe financial stress. One in seven organizations considered shutting down, and 63% foresaw a decline in income during the following year, of them 34% predicted the decline will be extreme. The falling income was due to reduction or discontinuation of allocations or donations, fluctuations in the dollar-shekel exchange rates, and a growth in operational costs. After thirty years of relatively fast growth of the Israeli third sector it seemed that a significant decline in size and strength of the Israeli Third Sector was looming (Katz and Yogev, 2009).

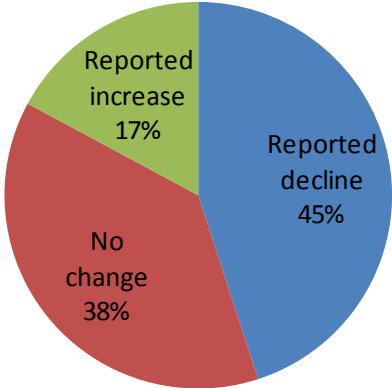
### **Momentary alarm or a real problem?**

The survey which was carried out a short while after the crisis begun, made us wonder whether the organizations were in real dire straits or was this no more than a panic reaction to the uncertainty of the times. To answer this question we carried out a second survey, a year later. The survey examined the state of 146 organizations of the organizations which participated in the first phase. Our findings from the second survey clearly show that the concerns caused by the first survey were justified. The findings reflected a real problem, and not just anxiety due to uncertainty brought on by the crisis. The situation as we see it from the current survey is that the Israeli Third Sector is facing a severe economic and philanthropic crisis, with consequences to its behavior and its capacity. A year and a half into the crisis, the number of organizations that reported a decline in their financial situation are double those who reported financial improvement. 45% reported that their financial situation has deteriorated in an average of 30%. In fact, the organizations were optimistic concerning their ability to face the crisis, when we compare their predictions in 2009 to what actually happened to them by 2010. The number of organizations who reported financial hardship in 2010 is almost double

the number organizations which estimated that they will have a problem overcoming the crisis a year before. These findings strengthen our understanding that the organizations evaluation of their situation was not mere panic, but rather an undervaluation of their situation.

Our first survey data showed that one in seven organizations were on the verge of shutting down: 13% had reported that they were considering completely shutting down the organization. In 2010 this inclination has lessened, but is joined by 4% of the organizations who have already shut down or are currently in the process. Hence, in 2010 15% of the organizations surveyed have either closed down or were considering doing so. In comparison to a the year before, the organizations' income flow has slowed down. More than half reported of a drop in total income (57%), of 30% in average. These data are higher than those reported in 2009, in which only 44% reported a reduction in income. Analyzing the source of revenue declines, we note that the financial crisis in the third sector can be described as mainly a philanthropic crisis – 74% of the organizations reported a drop of 30% in income deriving from philanthropy. Yet the decrease is not from philanthropy alone, but also from local and national government coffers: a third of the organizations reported an average of 52% drop in income from government. Income from sale of service is the only type of funding that more organizations reported a rise in (29%), as opposed to the number who reported a reduction (25%). The significance of the reduction in income is of course the undermining of the economic stability of the organizations. The survey clearly shows that the size of the organization influences its ability to withstand the crisis, and that it affects small and large organizations differently: only small or mid-size organizations shut down, were in the midst of closing or were considering doing so. The ramifications of small organizations shutting down are significant, since they are the sector's avant-garde, being easily able to reorient to new needs, demonstrate creativity and entrepreneurship (Kramer, 1988). These organizations are often involved deeply in advocacy, representing marginalized groups, who pay the highest price in times of crisis.

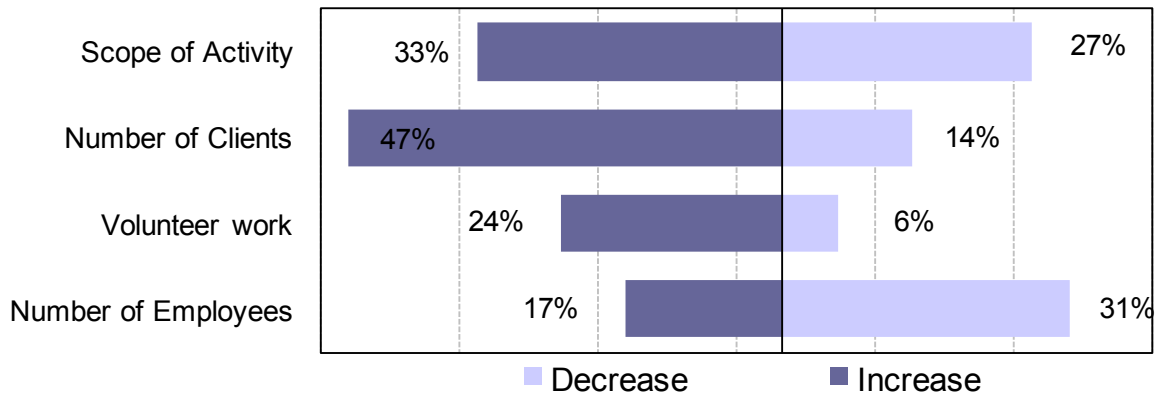
**Estimated financial capacity, 2009 compared to 2008**



**Doing more with Less?**

The economic crisis has impacted the citizens as well, increasing the number of people seeking services. Almost half of the organizations surveyed reported growth in demand for services. Yet, our data show that despite what seems to be a growing demand for services, the reduction in the scope of activities and the number of customers served is minimal. The survey portrays a situation in which the organizations are trying to do “more with less”, this paradox is apparent when one looks at the scope of employment. In almost a third of the organizations there was a decrease in the number of employees. On the average, these organizations lost a fifth of their workforce. The growth in the number of volunteers during the past year only partially offset this decrease.

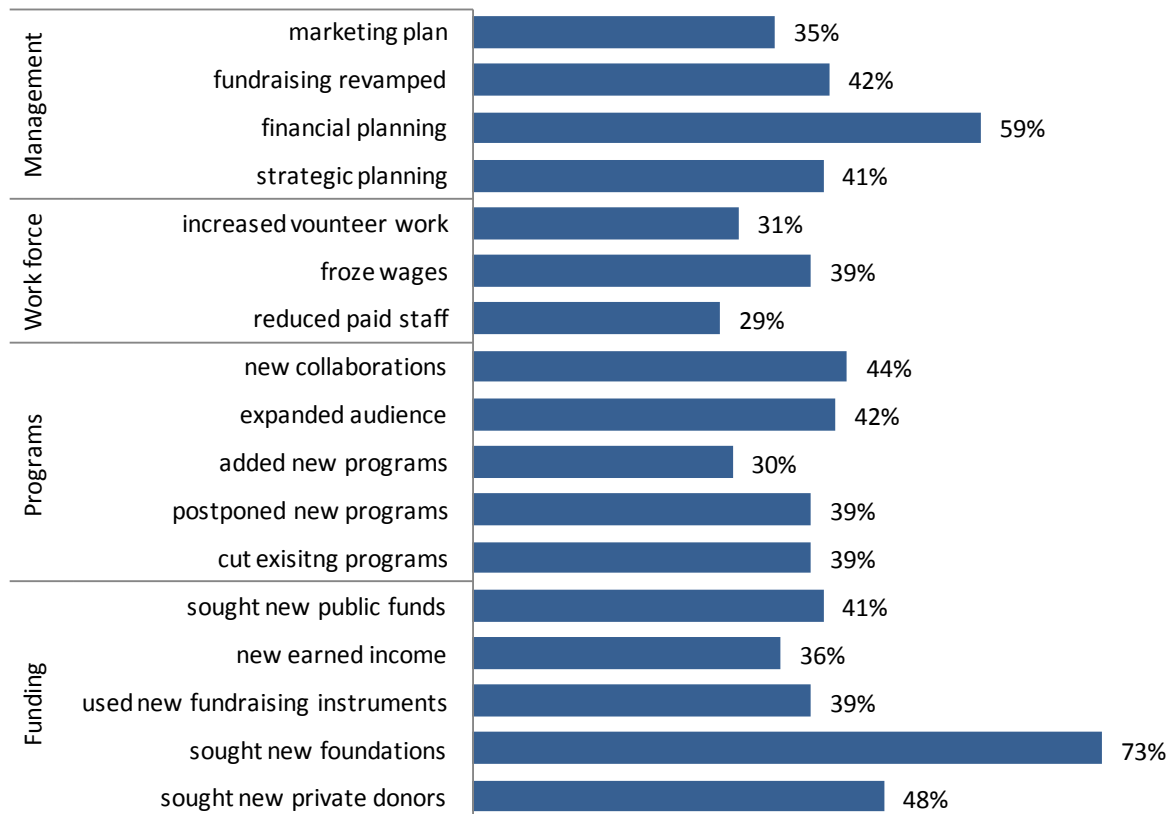
### Changes in scope, 2009



### Responding to the crisis

How did the organizations respond to the situation? The chart shows the major strategies that they used. Organizations sought fundraising from new individuals (48%) and foundations (73%), and tried new fundraising tactics (39%), and 41% searched for new channels of government funding. The attempts to tap these traditional sources of income seem particularly irrational, noting the sharp decline in both philanthropy and government support.

### Organizations' responses to the crisis



Another type of response that was prominent in our findings was an increase in the involvement of the organizations' boards in their organizations. In 28% of the study organizations it was reported that the board became more active in planning the organizations' resource mobilization program, and in nearly one in every five organizations board members are more involved in the actual spade work of fundraising itself. The rate of organizations whose board has a dedicated resource mobilization increased from 14% in our first survey, to 24% in the second one.

## Conclusions

The second phase of this study confirms the first phase conclusions that the crisis will bring considerable economic difficulties to Israeli nonprofits. Our findings and especially the comparison between the first and second surveys show that organizations find it difficult to foresee the future and prepare themselves with preventive measures. The question that arises is how long the organizations can "do more with less", raising serious concern over the seemingly inevitable result. It is difficult to estimate how long the organizations can survive in this scenario, and there is legitimate concern whether their devotion will cause them to spin to their demise. The difficulties can have far reaching consequences. These organizations serve populations the mostly don't have alternatives in other frameworks. The weakening of the organizations will in turn weaken their constituents.

Additionally, the smaller organizations, which are having the hardest time in this crisis, play an important role in generating social innovation and promoting social change, and their demise will hamper Israeli society's ability to develop new services, identify new social problem and offer new solutions.



ICTR was established at the Ben-Gurion University in 1997 in order to conduct and promote academic research and study on Civil Society, the Third Sector, and related fields in Israel. ICTR is a multi- and inter-disciplinary center at the Guilford Glazer Faculty of Business and management, serving researchers and students from academic disciplines, universities and colleges.

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