Foreword: toward a new economics

The US nonprofit sector, that diverse collection of hospitals, schools, soup kitchens, social service agencies, orchestras, museums, advocacy groups and many more, engages a paid workforce that is easily the third largest of any of the 18 industries into which economists typically divide a national economy, behind only retail trade and manufacturing. Also, with the full-time equivalent volunteer workforce included as well, this sector can legitimately lay claim to outdistancing any other single industry in terms of the scale of its workforce (Salamon 2012). What is more, this is hardly a unique American phenomenon. To the contrary, despite Western Europe's image as a 'welfare state', many European countries boast nonprofit-sector paid workforces that outdistance those of all but one or two other industries. Yet, despite this, the nonprofit sector has long been ignored as a meaningful economic sector and consigned to a backwater in economic analyses and in academic disciplines generally.

With the publication of the first edition of their landmark *Handbook of Research on Nonprofit Economics and Management*, Bruce Seaman, Dennis Young and their colleagues took a giant step toward correcting this situation. Now, with the publication of this second edition, they extend this contribution, updating and deepening much of the earlier analysis and adding to the range of topics they explore.

This is a rare volume, but its rarity takes at least three different forms. Indeed, other readers may well join this author in finding in this volume support for the insight advanced by exponents of deconstructionist literary criticism to the effect that any text has more than one interpretation. In the present volume, it is possible to find at least three distinct, though interrelated, messages, two of which are clearly present in the text and a third of which this writer finds suggested by it.

First and foremost, this volume provides a veritable cornucopia of fresh analytical insights into a societal sector that has long been popularly viewed through a heavy ideological fog. This constitutes a deconstructionist project of the first order. Few facets of nonprofit operations escape the analytical scrutiny of the skilled team of diagnosticians that Seaman and Young have mustered to examine this particular organism – not its sources of financial sustenance, its mobilization of workers, its pool of assets, its outputs, its patterns of interaction with other organisms, its internal organization, how it values its outputs, and how it comes to life or ceases to operate.

In each case, the authors bring a wealth of literature and analytical concepts to bear, many of them new to this particular field. They move beyond arid theory to test how well the theories fare in the rough and tumble of actual application as evidenced in the available empirical literature. As an encyclopedic bibliography of economic theory and empirical knowledge applied to these varied facets of nonprofit operation, the volume is an invaluable resource.

However, what makes this book rare is not just its consistently analytical insight and empirical rigor. Equally rare is its unabashed humility. Academics are notoriously prideful defenders of their respective disciplines as the most fruitful lenses through which to ferret

out the truth of various phenomena, but none may be more zealous defenders of the faith than economists. Yet here we have economists conceding that available empirical research cannot verify economic theories about some of the most basic features of nonprofit operations, such as whether diverse or concentrated revenue sources are best for long-term nonprofit fiscal health, whether government funding crowds out private giving, or why expectations from classical capital structure theories that equity should outdistance debt in nonprofit balance sheets fail to find reflection in the available data, to name only a few.

In explaining these disappointing validations of standard economic theories in the behavior of actual nonprofit firms, various authors identify two possible culprits. One is shortcomings in the available data, which limit the ability to test the economic theories adequately. The other is shortcomings of nonprofit management and nonprofit management literature in taking account of what the editors call ‘the thinking that economists can bring to the table’.

As far as the first is concerned, there certainly are limitations in available data. Form 990, the chief source of organizational data on the US nonprofit sector, was never designed to support serious economic analysis of nonprofit operations. The form offers limited data on the cost of capital, has its own classification scheme that does not align with that used in other economic data sources, is an organization-based dataset rather than an establishment-based dataset, and does a terrible job in clarifying the sources of nonprofit revenue, merging government grants with private philanthropy and government voucher payments with private payments for service. Among other things, this explains how two successive chapters in this volume can provide estimates of government’s share of nonprofit revenue in the US that diverge from each other by 100 percent (43 percent versus 22 percent). Similar problems exist in estimating nonprofit wage levels. One source of such data (the Bureau of Labor Statistics’ Quarterly Census of Employment and Wages) provides a fairly accurate picture of the extent of nonprofit employment but includes no demographic data on the employees, while another (the Census Bureau’s Current Population Survey) provides extensive detail on nonprofit employees, but relies on the employees to self-identify the sector in which they are employed. Is it not possible, therefore, that the reported finding from this latter source, that nonprofits have a workforce with more highly educated workers in more complex technical and administrative jobs than other sectors, could be an artifact of the fact that only the more highly educated of nonprofit workers are aware that they are employed by nonprofits?

Although these data issues are significant, it is far from clear that they could account for as pervasive a divergence between theory and reality as these chapters report. Nor can managerial incompetence or failure to imbibe the precepts of economics fully explain these deviations either. Nonprofit managers have performed remarkably well in growing their operations and adjusting to difficult fiscal circumstances during the very challenging past several decades (Salamon 2015). What is more, as the book’s editors note in their introduction to this second edition, practicing nonprofit managers and leaders apparently proved especially helpful in reviewing early drafts of the chapters in this book, making perceptive comments about nonprofit realities that several authors relied on in revising their initial drafts.

This brings us to what is perhaps the rarest feature of all about this volume, and is particularly valuable, even though it is more implicit than explicit in the text. This is the observation that the book’s authors may have been a tad diffident in reaching what may

be the book's most profound message. That message, in the opinion of this observer, is that whatever contributions the application of economic perspectives may bring to our understanding of the nonprofit sector, they may be overshadowed by the contributions that the study of the nonprofit sector can bring to the discipline of economics. Indeed, they may suggest the need for a more fundamental modification of the basic economics paradigm.

The starting point of economic analysis is always with rational actors free to choose among various alternatives, and always with the goal of making the most efficient use of resources. This perspective has already come under general criticism from observers such as the economic sociologist Mark Granovetter (1985), who faults classical and neoclassical economics for relying too heavily on 'an atomized, under-socialized conception of human action'. As Granovetter (1985, p. 483) puts it: 'Actors do not behave or decide as atoms outside a social context, nor do they adhere slavishly to a script written for them by the particular intersection of social categories that they happen to occupy. Their attempts at purposive action are instead embedded in concrete, ongoing systems of social relations.'

In its encounter with the nonprofit sector, however, the discipline of economics comes up against an entire sector of social institutions for which the appropriate analytical starting point is often a world apart from that conveniently assumed in economic analysis. Nonprofit organizations are frequently not free to choose among a broad set of revenue streams, as economic analysis of income diversity in the sector seems to assume as its analytical starting point. Funding options are often heavily constrained by the availability of different funding streams, the priorities of those with resources to give, and the alignment of organizational missions with the potentials for market revenue – all of these matters beyond the nonprofits' control. If the powers-that-be limit the development of government programs that fund nonprofit service delivery of benefit to the disadvantaged, nonprofits wanting to enter these fields are left to the mercy of those with resources, who may have little interest in such efforts. Resources generated by philanthropy, a system that allocates funds on the basis of one dollar one vote, are not likely to flow into the same channels as those directed by government support, a system that allocates funds on the basis of one person one vote. This throws a serious monkey-wrench into discussions of 'crowding out' that assume perfect replaceability of the two. Finally, discussions of why nonprofits can penetrate fields in which for-profits are operating misses the point that nonprofits are frequently the innovators in these fields and the real question is how and why for-profits manage to gain a toehold and, often, market dominance. The answer to this question often has more to do with the superior for-profit access to equity finance than it does with the heterogeneity of demand for services.

The growth and character of the nonprofit sector may thus be shaped more by these societal social and political circumstances than by the more abstract rational actor choices emphasized by the economics paradigm. That, at any rate, is the suggestion offered in a new volume seeking to explain the enormous variations in the scope and character of the nonprofit sector in a broad cross-section of societies across the world (Salamon et al. 2017). Once confronted with reliable, cross-national empirical data, it turns out that economic theories attributing these variations to heterogeneity in the preferences for collective goods on the part of individual citizens operating in free market economic systems and winner-take-all democratic polities simply do not begin to account for the actual variations that exist. Far more important than the preferences of individual consumers

and voters is the power of various social, economic, and political actors and groups. This suggests a different paradigmatic starting point for analyses of nonprofit development.¹

Interestingly, several chapters in this volume reach a similar paradigmatic conclusion. Thus, in analyzing markets with competition between for-profit and nonprofit firms, Brown and Slivinski take issue with the economic-theory explanations of the presence of nonprofits, noting that ‘nonprofits don’t just pop up automatically whenever the economic conditions are right’. Similarly, Toepler, in analyzing growing nonprofit engagement with government funding, points to the context within which these funding decisions take place, observing that:

Whether in industrialized or developing nations, philanthropic resources are generally very limited, whereas earned income strategies are either perceived as dubious or hampered by the lack of requisite institutions, such as functioning markets . . . For nonprofits the choices are, thus, to either pursue their missions incrementally on a relatively small scale or to look for alternative financial resources . . . For much of the second half of the twentieth century, nonprofits everywhere have opted to explore, and utilize, various forms of direct government support to scale up operations and reach additional clients, users or audiences for their work.

Finally, acknowledging the limited ability of standard for-profit asset management theory to explain the patterns of asset management performance among nonprofits, Bowman, Calabrese and Searing conclude that the problems result not from the inadequacy of nonprofit asset management practice but from the inappropriateness of the prevailing economic theories for understanding it. As they suggest: ‘The most important explanation for gaps in our knowledge is that much of nonprofit finance is informed by antecedent research on for-profit firms published in the business literature.’ They therefore call for a clean break from this existing economic line of thinking and the creation a ‘new theory devoted to nonprofit finance’, and specifically one that starts from the realization that nonprofits, unlike for-profit firms, operate from a ‘dual bottom line’.

This line of thinking currently has particular relevance precisely because of the growing power of commercial impulses within the nonprofit sphere (Salamon 2015). With government resources constrained or in actual decline and philanthropic ones barely growing, nonprofits find themselves forced increasingly into commercial forms of operation. This marketization of the sector has been joined, moreover, by the rise of what might be termed managerial professionalism, the penetration of business management practices into the operation of nonprofit firms.

While these developments have important positive consequences, they are in danger of eviscerating the very qualities that make nonprofit organizations special, giving rise to a phenomenon much discussed in sociological circles but curiously missing, or not such a source of concern, in economic circles – namely, institutional isomorphism, the obliteration of meaningful institutional differences between nonprofit and for-profit firms (DiMaggio and Powell 1983). That is, far from viewing the penetration of economic thinking into the operation of nonprofits as a development to be encouraged, sociologists, political scientists and nonprofit managers have come to see it as a problem to be confronted. At the very least, to the extent that we value a set of institutions that gives primacy to what might be termed ‘nonprofit-ism’, that is, the private pursuit of public purpose without undue regard for purely economic rewards, this trend should be a cause for concern (Salamon 2015).

What this suggests, at a minimum, is a greater recognition of the legitimacy of the nonprofit sector's double bottom line as the starting point for economic analysis of this sector's operations and performance. However, this shift in paradigm may be applicable to the discipline more generally. Powerful forces are underway internationally that seek to move the economics frame of reference in a similar direction. One evidence of this was the report of the well-known Stiglitz Commission, convened by French President Sarkozy, which articulated a new framework for economic thinking keyed to the concept of 'well-being' rather than the more narrow concept of 'gross national product'. These ideas have begun taking institutional form in the emergence of new 'social enterprises' that merge market means more explicitly with social and environmental ends. European policy circles have been particularly attentive to these developments. In a 7 December 2015, 'Conclusion', the Council of the European Union (2015) referred to this emerging 'social economy' as a 'key driver of economic and social development in Europe'. As the Council noted: 'Social economy enterprises . . . include organizational forms such as cooperatives, mutual[s], foundations, and associations as well as newer forms of social enterprises . . . whose main purpose is to create a positive social impact' (Council of the European Union 2015). Moreover, this is not simply a fringe development. Many main-line corporate enterprises have also been bitten by this same social-purpose bug, as evidenced by their embrace of the nonprofit notion of an organizational mission statement that goes well beyond the simplistic goal of maximizing profit. And this perspective has even jumped the divide into the capital markets arena with the emergence of a 'new frontier of philanthropy' that involves the mobilization of private investment capital into social and environmental problem-solving (Salamon 2014).

In summary, with its efforts to test the applicability of economic concepts to the world of nonprofit operations, this book may ultimately find itself contributing to something bigger: the construction of a 'new economics'. If so, it may be just in time.

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NOTE

1. The authors of this analysis suggest what they term the 'social origins' theory as a more empirically valid starting point for explanations of the scope and character of the nonprofit sector around the world. This theory blends comparative history, sociology, political science and economics in explaining the constellations of factor that account for the widely variant patterns of civil society development on the global level. See Lester M. Salamon, S. Wojciech Sokolowski and Megan A. Haddock, *Explaining Civil Society Development: A Social Origins Approach* (Baltimore, MD: Johns Hopkins University Press, 2017).

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