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Risky business? The survival implications of exploiting commercial opportunities by nonprofits☆

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ABSTRACT

Prior research is equivocal as to the performance implications of exploiting market-based opportunities by nonprofit organizations. We investigate an under-addressed measure of performance in this literature: organizational survival. Drawing upon resource dependence theory, we argue that performance is largely dependent upon the extent to which nonprofits focus on market-based opportunities. Through analysis of the population of Canadian charities, we find support for a U-shaped relationship indicating that low to moderate levels of market-based income decrease the likelihood of firm exit, whereas high levels increase this likelihood.

1. Executive summary

Social entrepreneurship refers to the process of creating social value through market-based means (Austin et al., 2006; Mair and Martí, 2006). This process spans varying organizational forms, such as nonprofit, for-profit, and hybrid organizations. Given that nonprofit organizations (NPOs) are inherently social, scholars have established that social entrepreneurship in this sector occurs when NPOs generate part of their income through the sale of products or services (Boschee and McClurg, 2003; Kerlin, 2005; Thompson, 2002; Wallace, 1999).

Whether or not the generation of market-based income by NPOs is holistically beneficial or detrimental to the organizations has remained a contested subject. Advocates of the practice argue that market-based income is beneficial for these organizations as it provides supplemental funding, income stability, and self-sufficiency (Brinckerhoff, 2000; Carroll and Stater, 2009). Conversely, opponents argue that market-based income generation distracts NPOs from achieving their social aims, creates cultural conflict, increases financial risk, and threatens legitimacy (Dees, 1998; Foster and Bradach, 2005). In this study, we seek to reconcile the two conflicting views by uncovering how market-based income generation affects the survival rates of NPOs.

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Our theoretical arguments are based upon resource dependence theory (RDT), which maintains that organizational survival depends on the organization's ability to acquire resources (Pfeffer and Salancik, 1978). According to this theoretical perspective, NPOs engage in market-based income generation to manage their dependency on government grants and private donations as sources of funding. As such, the addition of an alternative funding source—market-based income—should stabilize their flow of financial resources, increasing their survival chances. However, RDT also suggests that attempts to manage dependence may result in a shift of dependence patterns. Based on this logic, we propose that when NPOs generate high proportions of market-based income, their dependence shifts to commercial markets, decreasing their survival chances. We empirically test our hypotheses with data on all registered charities in Canada between the years of 2005 and 2010. The sample includes NPOs with a variety of social missions, such as poverty relief, education advancement, religion advancement, and other charitable purposes that benefit the community. Given our research question and the nature of the data, we employ Cox proportional hazard models to test our hypotheses.

The results of this study contribute to the nonprofit and social entrepreneurship literatures by reconciling the two views regarding the effect of market-based income generation on NPO performance. Specifically, we found a U-shaped relationship between the proportion of market-based income and the probability of NPO exit. This result suggests that whether market-based income has a positive or negative effect on performance is based on the extent to which such income in pursued. That is, at low levels, market-based income is beneficial for the NPO, yet at high levels, it becomes detrimental to survival. Understanding these results can aid nonprofit entrepreneurs in crafting optimal market-based income strategies.

2. Introduction

Until fairly recently, there existed little research at the intersection of the entrepreneurship and nonprofit domains. Indeed, the very mention of entrepreneurship, profits, sales, and the like were once shunned by the nonprofit community (Foster and Bradach, 2005; Weisbrod, 1998). However, in the 1990s, a 'perfect storm' of circumstances detrimental to the survival of nonprofit organizations (NPOs) was brewing. Namely, increased competition among NPOs, decreased government funding, a shortage of grants and donations, rising costs, and increased rivalry from for-profit competitors forced nonprofit managers to become more entrepreneurial in how they conducted themselves (Dees, 1998; LeRoux, 2005; Morris et al., 2007). In particular, NPOs began seeking more market-based opportunities, the exploitation of which would yield funding through the sale of goods and services (Dees, 1998).

Research on the topic soon followed, often under the banner 'social entrepreneurship.' Social entrepreneurship, in fact, is frequently defined as the generation of income by NPOs through commercial means (i.e., profits from sales of goods and services; Boschee and McClurg, 2003; Kerlin, 2005; Leroux, 2005). Soon after and within this stream of research, a rich debate manifested among scholars as to the consequences—both positive and negative—of pursuing market-based opportunities. On the positive side of the ledger, scholars argue that market funding can provide supplemental income, income stability, and self-sufficiency (Brinckerhoff, 2000; Carroll and Stater, 2009; Dees, 1998). As such, scholars in this camp generally contend that entrepreneurial behavior has a positive effect on the performance of NPOs. On the negative side of the ledger, being more businesslike can distract organizations from achieving their social aims, create cultural conflict, increase financial risk, and threaten the legitimacy of the organization (Dees, 1998; Foster and Bradach, 2005). Scholars in this camp generally assert that entrepreneurial behavior has a negative effect on the performance of NPOs. While the debate is far from settled, a review of the extant literature indicates that a greater number of scholars adhere to a 'the more the merrier' approach to market-based income generation than the converse.

We advance research in this debate in three primary ways. First, drawing upon resource dependence theory (RDT), we synthesize the arguments of both camps into a coherent premise that demonstrates the consequences of entrepreneurial behavior by NPOs. Specifically, we argue and find support for a curvilinear relationship indicating that market-based income is significantly beneficial at low to moderate levels yet is harmful at higher levels. In doing so, we demonstrate that the suppositions of the two camps are not mutually exclusive but are instead conditional upon the extent to which market-based income is generated. Second, empirical rigor has largely remained absent in generating conclusions on the topic. While findings from case studies, small samples, and cross-sectional data have yielded informative results, we believe that more extensive empirics may add valuable fidelity to extant conclusions. We conduct a large-scale longitudinal analysis on market-based income and organization-level outcomes of NPOs. Our analysis is carried out on the population of registered charity organizations in Canada between 2005 and 2010. Data are drawn from the tax forms filed by these charities each year with the Canadian government, which both lends support to the validity of the measures and allows us to control for several critical factors that may account for variance in income streams and outcomes. Third, whereas much prior work on the effects of income sources focuses on outcomes like total revenue or variance in revenue (e.g., Carroll, 2009; Carroll and Stater, 2009; Kingma, 1993), we focus on a salient yet under-researched outcome: organizational survival. As the accomplishment of an organization's mission is first predicated upon the existence of the organization, we view organizational survival as a particularly relevant topic for NPOs—one worthy of greater scholarly attention.

The contributions of this study are both theoretical and practical. With regard to theory, we explicate a solution to the ongoing debate of the benefits and detriments of exploiting market-based opportunities by NPOs—one that incorporates both vantage points. With regard to practice, we offer some guidance as to the levels at which market-based income shifts from valuable to dangerous.