ges of the Fund, it may well be important for the UNCF to keep its mis-
on statement this narrow, to explicitly prevent themselves, for example,
om soliciting for other Black colleges, currently not among the members.
lofsky has argued that nonprofit organizations with stable, narrow goals
ll find it easier to recruit individuals to articulate and support those goals
the broader community.[20] These observations, of course, bring us back
the key point articulated earlier:

The mission statement has a function for each of the organizations' constituents. Changes in that mission come about because either the environment changes or the needs of one or more of the constituents change.

In one of the cases in this book, People for the American Way, the
estion of when and how a mission should be broadened is raised. The
estion is a difficult one for all evolving organizations.

nclusion

this chapter, we have considered the ways in which the mission of a
nprofit organization comes from its core competitive advantages. I have
gued that nonprofits tend to focus on their missions because of several
aracteristics of their structure. We typically think of this emphasis on
ssion as a plus; indeed, the Drucker quote cited in Chapter 1 is quite
datory on this point. The focus on mission in the nonprofit sector,
wever, can also have a dark side. For some organizations, discussions of
ssion are used to cloak inefficiency, or a job poorly done. Nonprofits that
in financial trouble often retreat to discussions of the mission when
cussions of management control systems, fundraising, and accounting
stems might well be more useful. We sometimes see an organization
ating a kind of cocoon of its mission, clinging to an outdated mission,
en in the face of radical environmental upheaval.

Thus far, we have depicted the mission statement largely as a visionary
cument. To succeed, however, an organization needs a set of goals that
only embody the vision of the constituents, but make some sense in
ms of the realities of the economic marketplace and the political and
ial environment. In the next chapter, we will consider some of the tools
t an organization in the nonprofit area can use to understand its envi-
nment.

3

Structural Analysis of a Nonprofit Industry

Nonprofit organizations often begin with a vision. To survive, however, organizations must also understand the economic and political markets in which they operate. The importance of hard-headed market analysis and good management in running a nonprofit is made well by Franklin Thomas, president of the Ford Foundation, the largest philanthropic foundation in the world: "People think of (nonprofits) as soft, imprecise, and touchy-feely. That's just malarkey. Invariably when businessmen come over to this side, they say they never imagined it to be so hard."[1]

In this chapter, we will focus on an analysis of nonprofit markets. What are the salient characteristics of markets that help determine the success or failure of a nonprofit venture? How do we analyze demand and supply in nonprofit markets? What are the key success factors for organizations in those markets? As we answer these questions, we will begin to form a picture of the markets in which nonprofit organizations operate, and the tools available to help nonprofits manage in those markets.

Competitive Analysis for the Nonprofit: The Industry Level

We begin our analysis by looking at the market in which a sample nonprofit organization currently operates. Is it a market with fierce competition from other organizations? Are there good substitutes from other public or private-sector products or services? Are the donors to this organization powerful or diffuse? How likely is it that new firms will enter this market? The answer to these questions help to determine how easy it is for an organization to succeed in its market.

One helpful way to organize our discussion of the current condition of the industry is by using a *Six Forces Diagram*, adapted from a similar diagram developed by Michael Porter for the corporate sector.[2] Figure 3.1 is a

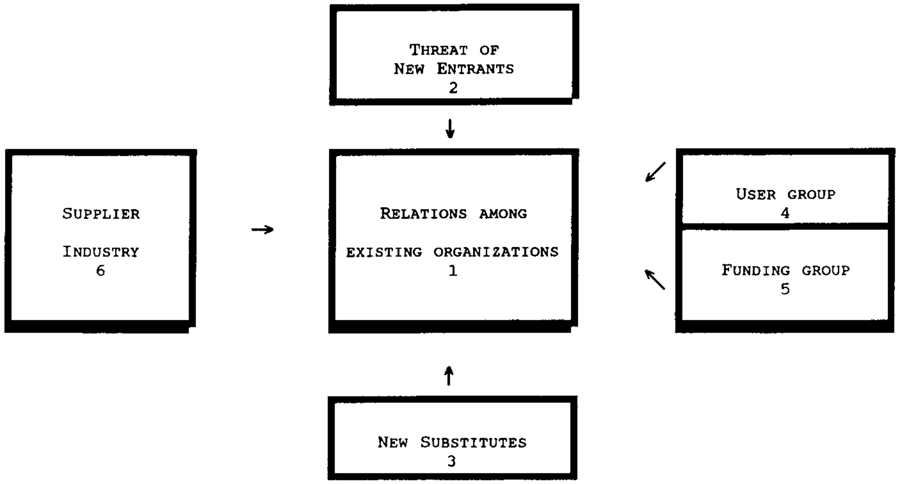

Figure 3.1. Six Force Chart for Nonprofit Industry Analysis.

schematic of the Six Forces analysis. In the discussion that follows, I have applied this model to the United Way to give some flavor for the way in which it might be used by a nonprofit.

Market Definition

Before we analyze the industry an organization is in, we must know what that industry is. Saloner has argued that the first element in any organization's strategy is a statement of the *scope* of that organization, a description of the activities it is engaged in and the market in which those activities are embedded.[3] In the corporate world, we call this the *market definition* task. Is Bumble Bee in the tuna market, the canned goods market, or in the food market? Is the Santa Fe Opera House in the classical opera market, the music market, or the tourist trade? Is the YMCA in the business of character development or athletics? Often, we will look to the mission statement to get a first cut on the way an organization sees its industry. It is a first cut only, however, and many organizations spend considerable time trying to decide just what their market definition should be.

In the case of the United Way, we will take their mission statement as a guide to market definition in order to apply the Six Forces analysis. The United Way is a collection of more than 2,000 local affiliated operations designed to organize workplace solicitation and distribute funds raised in the workplace to local charitable organizations. In many regions of the country, the United Way grew from the Community Chest operations. Its stated mission is "to serve as a single, communitywide, voluntary fundraising or planning agency; to increase a community's organized capacity to give." The primary method of fundraising used by United Way throughout the country has been workplace solicitation. Thus, at least for now, we

will define the industry of United Way as "fundraising in the workplace for community-based agencies."

Description of Current Industry Participants

Once we identify the market, as we have done for the United Way, the next task in an industry analysis is to describe the existing relations among organizations in that market. This area is covered in box 1 of Fig. 3.1, in the center of our picture. Are there a great many organizations that share the market or are you more-or-less alone? If there are other organizations in the market, can you identify them, either individually or as types?

The first task of an industry analysis is to develop an inventory of the other organizations currently in the market and the characteristics of those organizations.

In general, market attractiveness decreases with the number of competitors. Diversity among competitors increases market attractiveness.

Competition for donors, clients, and staff are all reduced in markets with few rivals. Moreover, these markets provide more coordination opportunities than do denser markets, and coordination typically improves a firm's ability to survive. Diversity allows organizations to specialize in particular niches and also avoid head-to-head competition.

In the corporate world, our normal expectation is that organizations that share the same industry will be competitive vis-à-vis one another. Thus, in looking at the central box in Fig. 3.1 we can largely confine ourselves to a structural analysis of the number, size, and character of the industry participants. In the nonprofit area, the analysis is more complicated for we often see more cooperation among firms. Thus, in addition to the structural analysis of how many and what kind of organizations are in the industry, in nonprofit markets we will typically also want to know something about the nature of relations among those organizations. Museums, for example, share parts of their collections through traveling exhibits. It is not uncommon for administrators of schools to meet regularly to discuss both pedagogic and business issues, though as we will discuss in the later chapters, some attention must be paid to antitrust laws governing these areas. Relief and development organizations like Save the Children and Oxfam often cooperate in programs involving airlifts of food. In Chapter 4, we will pursue further the question of cooperation versus competition among nonprofits. For now, I simply want to indicate that even if there were a considerable number of organizations within an industry, the level of competition need not be intense and our analysis should probably go beyond the structural level to indicate something about the level of cooperation, if any, in the market.

Task 1 of an industry analysis is to create an inventory of competitors, and a characterization of any existing cooperation among those competitors.

In the United Way example, this first task is relatively easy. In the past, the United Way has had virtually a monopoly on workplace solicitation, and it still maintains this monopoly in many areas. Thus, in the central box of our United Way Six Forces diagram I would characterize existing rivalry in the industry as *modest*, although I would note that even now in some areas of the United States, the level of competition is growing.

Entry Conditions

Consider now the top box of Figure 3.1, box 2, marked *threat of new entrants*. Here we turn in our analysis to look at the future. How many new competitors are lining up around the industry and what are their characteristics? What are the major *barriers to entry* into the industry? How high are those barriers? If barriers are high, the organization can expect little change from new entrants; with low barriers we often see considerable volatility in a market. Knowing about entry barriers helps nonprofit managers gauge the amount of change they can expect in an industry.

The idea of entry barriers comes directly from the for-profit sector and requires some adaptation if it is to be useful here. An *entry barrier* is defined as any "phenomenon which permits incumbents to earn supra normal profits on the whole process of getting into the market and continuing to act, without inducing others to enter and bid those profits away."[4] Typical entry barriers in the corporate sector include economies of scale, sunk costs, marketing and/or research experience, and reputational affects. The presence of one or more of these phenomenon can protect a firm from new competition, competition that will eventually reduce prices and erode profits.

We clearly cannot rely precisely on this definition of entry barriers with its focus on supranormal profits when we think about the nonprofit sector. Nevertheless, it is clearly important in the nonprofit sector to get some measure of how protected the organization will be from other organizations trying to enter the same market. I would propose the following definition of entry barriers for use in the nonprofit sector:

An entry barrier in the nonprofit sector is any phenomenon that prevents new organizations from entering the market and serving that market in an economically viable way.

In identifying entry barriers, we look for features of the market that allow existing firms to survive but keep other firms out. Note the reference to "economically viable" in the definition. In the nonprofit sector, such viability is created by revenues generated from fees, grants, or donations. We are thus looking for factors that make a particular venture viable for one organization and yet leave no room for rival organizations.

A second important feature of the entry barrier definition is the focus on the *differential* impact of a given factor. For example, the fact that a particular activity is hard to sell via a fee is not in itself an entry barrier. This feature of the market is certainly a problem, but it is one that potentially affects existing firms as well as new firms. On the other hand, if existing firms have long-term contracts to supply that service for a fee, then this contract is an entry barrier, inasmuch as it hurts new entrants but not old. This distinction should become clearer as we examine particular examples of entry barriers.

What are the principal entry barriers we see in the nonprofit area? If we consider for a moment the kinds of goods and services produced in the nonprofit sector, then it is clear that a major entry barrier in many of these markets is *reputation*. Indeed, as we argued in the last chapter, nonprofit organizations arise in many sectors because they engender trust in either donors, government agencies, or clients. Well-established nonprofits, however, are typically more able to engender trust than would newcomers to the field. In markets in which fundraising is important, this entry barrier is likely to be most important.

The importance of reputation as an entry barrier helps to explain some of the organizational patterns we see in the nonprofit area. In the nonprofit area, geographical expansion of a good or service typically occurs through a kind of franchise system, in which a national organization lends its name to a network of local affiliates.[5] This pattern occurs because of the high value that the brand name has in the nonprofit area. It also suggests that nonprofits may need to be more concerned about rumors of misbehavior than the for-profit sector. Nonprofits are held to higher standards precisely because reputation plays such a central role in the allocation process.

Reputation is the major entry barrier in most nonprofit markets.

A second entry barrier we see in some parts of the nonprofit world is *access to distribution channels*. For organizations that do workplace solicitation—like the United Way—privileged access to corporation payrolls is a formidable barrier. Relief projects that work through religious organizations have a similar advantage in fundraising because they can use the distributional network of the Church. In some areas of the world, Catholic Relief Services, for example, has advantages over other relief operations because it can tap church connections to administer its programs as well as for fundraising.

Access to distribution is an important entry barrier for many nonprofit markets.

Scale Economies are one of the most important entry barriers in the for-profit world, and they sometimes play a role in the nonprofit as well. Economies of scale exist whenever unit costs fall as an organization expands its scale of operation. When economies of scale are substantial, the size of the investment required of a new entrant increases. This, in turn, raises the risk of entry and thus discourages new entry. In this way, an entry barrier is created.

In manufacturing operations, scale economies come principally from the opportunity to use more advanced technologies as scale increases. In service industries, scale economies come from increased opportunities for labor specialization. A large museum can employ a specialist in many different periods; a smaller one may need to meld together curatorial functions and business functions. Being able to use specialists may allow the museum to mount the kind of show which will attract both audience and donors, a show that is beyond the abilities of the smaller operation, even if it has extensive gallery space. Blau et al., in their analysis of performing arts organizations, argue that the ability of large arts organizations to attract volunteers and unpaid artists lead to an economy of scale in the paid staff.[6] Large schools can spread the costs of a library, gym, school nurse, and the like over more students and thus achieve lower costs in this way. Large community-based hospitals can have advantages over small rivals because of their ability to efficiently spread costs of specialized personnel and equipment. The Centers of Excellence run by Humana Hospitals in which a facility is devoted to a particular specialty and patients come from far and wide to be treated in that facility is another example of an organizational structure designed to exploit scale economies.

Scale economies are another entry barrier in some markets.

A fourth source of entry barriers is *government regulations*. In a number of industries, entry is controlled by government. Liquor stores in many states, for instance, require state or local licenses to sell their wares. In a number of cities in the United States, taxicabs require medallions as a prerequisite to operation. Patents often prevent firms from copying product or process innovations developed by their rivals and thus reduce entry. In the nonprofit world, government regulation via licenses and certification often play a role in deterring entry. Hospitals must obtain certificates of need in order to invest in certain specialized capital equipment. In most states, nursing homes and day-care centers require licenses in order to operate. In the case of LEEWAY, the hospice for AIDS patients in this text, we see some of the effects of these licensing regulations on entry. In some regions of the country, fundraising is subject to various restrictions. The American Red Cross in many localities has been granted monopoly control over blood collection. In each of these areas, state, local, or federal government rules influence entry.

Government regulation controls entry in many markets.

The last entry barrier I will discuss is the presence of *specific assets* in the conduct of business. Every firm considering entry into an industry must simultaneously consider the costs of exiting that industry. For small businesses probabilities of exit are extremely high. In 1985, for example, half as many small businesses failed as started.[7] Mortality rates for nonprofits are also quite high, again particularly for smaller ones. Forty percent of the nonprofit organizations currently in operation were started in the last twenty years. If failure is possible, however, then new entrants into a

market will need to consider the costs of that failure. The higher are the costs of failure, the less likely new entry will be. It is here that specific assets play a role.

An asset is specific to market if it cannot be used to increase value or reduce costs when applied to another market. Large specific assets increase entry barriers.

If I have to invest in a specific asset in order to enter a market and that venture fails, then my full investment is wasted. This is clearly a less-attractive market than one in which I can move my assets from one failed market to a second, more promising one.

What are examples of specific assets? Production facilities are often quite specific. Thus, an oil pipeline from Prudhoe Bay, Alaska, to Valdez is a very specific asset. Once the oil is gone, the pipeline will have no use. Church buildings and university facilities are often thought of as quite specific assets; thus, it is often difficult to raise capital using these facilities as collateral. Banks recognize that if the church fails, then its building will not be worth very much. Nonprofit organizations that carry most of their balance sheet operations in their buildings and plant account are typically quite vulnerable, precisely because the specificity of these assets makes them difficult to liquidate in hard times. Very specific knowledge, networks, and relationships developed by the principals in an organization are also often specific assets, not very useful in other ventures. Decisions to invest in these assets are not made casually.

The existence of specific assets discourages entry by raising exit costs.

I have now described the five main entry barriers seen in the nonprofit world. They are summarized in Figure 3.2. Let us turn to the United Way and examine entry threats in its market.

For the United Way, analysis of the entry conditions is quite revealing. In 1980, less than $1 million was raised in workplace solicitation outside of

REPUTATION AND IMAGE

ACCESS TO DISTRIBUTION

ECONOMIES OF SCALE

SPECIFIC ASSETS NEEDED

GOVERNMENT REGULATION

Figure 3.2. Barriers to Entry for Nonprofits.

United Way auspices. By 1990, the figure was close to $10 million, and rapidly growing. In many parts of the country, the Combined Health Appeal—a fund raising unit for most of the disease research funds—has launched a major challenge to United Way. In other parts of the country, organizations, including many state agencies, are allowing their employees to designate any nonprofit to receive workplace contributions, effectively overriding the United Way role. What were the factors that historically protected the United Way so effectively and what is eroding those barriers?

In the workplace solicitation market, the three principal entry barriers are access to distributional channels, reputation, and specific assets in the form of network building. While each of these barriers remains substantial, there has clearly been some erosion in their overall magnitude.

In this market, the major change has been in the importance of distributional access, or more precisely in the difficulty of gaining such access. With the increased sophistication of corporations in their information systems, firms can now essentially conduct their own campaigns, in which employees have wide latitude on designation of recipient charity. Large firms like Xerox and state government organizations have led the way in this area, and it is a trend that is likely to continue.

The role of reputation in the workplace solicitation market, on the other hand, seems undiminished. Thus, most of the competition in the area has come from other organizations—like the Combined Health Appeal—that also have substantial reputational assets. Unfortunately, the United Way's own reputation suffered substantially in 1992, with the widespread discussion of the high salary of William Aramony, the head of the national organization, and allegations of misuse of power.

There have also been changes in the power of the United Way networks. For most United Ways, the strength of the networks has been in the manufacturing area. In many parts of the United States, however, manufacturing is losing employment. Thus, while the importance of networks as entry barriers remains, the value of the specific networks developed by many local United Ways is beginning to crumble. This, too, has contributed to the diminished power of the United Way versus new competitors.

Competition from Substitute Products

Thus far, we have described the threat to existing organizations from current rivals in the same market and from potential entrants. Organizations, however, are also affected by competition from related markets. We cover this area in box 3 of the Six Forces diagram, *substitutes.* Air conditioners compete with fans, disposable diapers with cloth, opera with musicals, and dramatic theater and public television with videos. In all of these cases, the availability of substitutes influences the ability of an organization to charge fees for its goods or services and to raise donations to cover its costs.

Readily available substitutes reduce an organization's ability to attract either donors or clients.

How do we identify those products and services that are substitutes for our own? In part, this returns us to the market definition task we discussed earlier. Here, we wish to identify products and services that serve more-or-less the same function to more-or-less the same people as our own. This process of identification can clearly be a subtle task and one that requires both analysis and imagination.

In some cases, it is possible to use statistical analysis to shed some light on the degree of substitution among goods or services. Gapinski, for example, uses data from London to examine how attendance at theater, opera, symphony, and dance events are influenced by the prices of one another.[8] How does the price of opera tickets, for example, influence theater attendance, holding all else constant? This effect is known as the *cross elasticity of demand,* and is a measure of substitutability across entertainment types. For Gapinski's sample, symphony and dance attendance appear to be very sensitive to theater and opera prices, while the patrons of theater and opera are less influenced by prices in the other lively arts. Thus, dance and symphony companies may need to track the prices of the other arts quite carefully, where theater and opera companies appear to compete primarily within their own niches.

What are the substitute products in the case of the United Way? Solicitation at home, via direct mail or other appeals, is clearly an important competitor to the workplace solicitation done by the United Way. Indeed, as direct mail fundraising has become more common, it has become more of a threat to the United Way's efforts.

The Demand Side

The right-hand side of the Six Forces diagram contains the "customer" part of the picture, what economists might call the *demand side.* For nonprofits that depend on fundraising, there are two classes of customer. First, there are the users of the good or service. We cover this in box 4 of Figure 3.1. For many nonprofits, these users will be one revenue source, through collection of fees-for-service. As we indicated, however, most nonprofits are not strictly fee-based and thus the nonprofit must look to the second "customer," the donor, in box 5 of the picture. To this customer, the nonprofit is selling the peace of mind that goes with giving to a good cause, or the prestige of having one's name on a patron list, or whatever service these donors are seeking. In doing its competitive analysis, the nonprofit needs to assess the power of both its users and its donors.

For the "donative" nonprofit, like Save the Children or Greenpeace, which rely principally on donors, box 5 will be paramount. For commercial nonprofits, like the Educational Testing service and most hospitals, box 4 will dominate.[9]

Users

All businesses—for-profit or not-for-profit—need to pay attention to what their customers want. Nevertheless, there are considerable differences among organizations in terms of how powerful buyers are, on just how much attention they need. What are the factors that increase the power of the buyer group?

First, we look at the *number* of buyers and the distribution of their purchases. For the local Red Cross, which sells blood to hospitals, the individual hospital may have considerable control, particularly in areas served by only one hospital. This is a very different situation from that facing the Chicago Art Institute as it considers the power of its customers, art visitors, and art students. For the Art Institute, while it cares about its audience as a whole, no one or two particular customers wield much influence.

The more concentrated are the clients or customers of a nonprofit, the more control they will wield. A measure of concentration is the fraction of services used by the top three or four clients of the nonprofit.

The second major consideration in determining the power of the buyer is whether the buyer can produce the good or service himself or herself or turn to other suppliers. We have already covered the importance of substitute producers in boxes 1, 2, and 3 of our diagram. In some cases, however, even with no substitutes available, buyers can create their own substitute by *vertically integrating*. Individuals who want to learn emergency water safety cannot do this themselves; they need an intermediary like the YWCA or the Red Cross. On the other hand, the hospitals to which the Red Cross supplies blood may have a plausible threat that they could integrate backward into the blood collection function. In the late 1980's, the then-president of the United Negro College Fund, Christopher Edley, acknowledged that several of the Fund's strongest member schools had threatened to withdraw from the consortium to raise money on their own.[10] This threat clearly influences the strategy of the Fund vis-à-vis its members. One might argue that the Catholic Church developed more power than the typical Protestant denomination because the individual is less able to produce his or her own religious experience in the former case than in the latter. In this sense, Martin Luther challenged the power of the Church in a quite profound way by augmenting the power of the buyer by increasing his or her ability to vertically integrate.

Customers gain power when substitutes for the service are available, or self-production is possible.

The last element to look at in evaluating the power of the buyer is how important the good or service is to that buyer. The more important the good or service, the more the buyer will invest in making sure he or she is well treated. Hence, the more power the buyer appears to have. As education becomes more important to parents, for example, they become more powerful buyers in the private school market. It is not uncommon these days to hear private school administrators in areas that service highly academic parents to describe parental attitudes as "consumerism." Here, administrators are clearly responding to the power of the involved buyer.

Customers are more powerful when the product or service they consume is very important to them.

This latter point is particularly important given the political nature of many nonprofit operations. One way customers gain power in the nonprofit sector, even when they are relatively diffuse, is by banding together. The costs of collective action, however, are typically relatively high, and thus such action will only be taken in selective cases.

For the United Way, the users are the many local organizations that depend on it for their fundraising. These users provide no funds directly to United Way, but they are nevertheless quite important from a fundraising perspective because, at least to some extent, it is the composition of this user group that determines the strength of the United Way's pull to donors. Understanding this group, and the alternatives they have for coordinated fundraising, is thus essential for the United Way.

How much power do these groups have? In most communities, the number of groups served by the United Way is large; the pattern is one of many small users, rather than one or two large ones. In general, organizations served by the United Way have had limited ability to integrate backward and do workplace solicitation themselves. Here, too, we see limited buyer power. On the value dimension, the assessment is mixed. Some organizations do rely heavily on the United Way. It is interesting to note, however, that at least some local United Ways have policies that limit the share of an organization's revenues that can come from United Way. The effect of this policy—however disinterested its cause—would clearly be to limit buyer power.

Thus, in the past, organizations served by the United Way—especially the smaller ones—have had relatively little power vis-à-vis United Way. Given United Way's current monopoly in the workplace, most of these groups have no place else to turn should United Way offer an unappealing bargain. The picture, however, is not all good for the United Way, for while no one organization can integrate backward into workplace solicitation, groups of organizations, united by area of concern, can serve themselves and increasingly seem to be doing so. For some organizations, the importance of workplace solicitation has been large enough to induce collective action to challenge the United Way. The Combined Health Appeal, for example, is an umbrella organization serving the American Heart Association, the American Cancer Society, and so on, that has entered the workplace market in a very powerful way. The Black United Fund similarly pulls together organizations and allows them to jointly pose a threat that none could mount on its own. In sum, while the power of buyers has historically been low for the United Way, it is growing.

Donor Power

For the typical nonprofit organization, there is a second group on the demand side of the market, the donors. Here, too, we can do a structural analysis to determine how much power is held by this group. We begin by asking: Who gives to the organization? Are there many small donors or a few large ones? Are they concentrated regionally? Are donors corporate, individual, or the state? How much power does each have? As with the user groups, the more numerous the donors and the less the average gift, the less power each donor has.

The power of the donor typically increases with his or her share of revenues.

We see this effect clearly in the museum market. For museums like the Whitney Museum in New York and the Getty Museum in the Southwest, much of the business revolves around the collections, resources, and views of a few important donors. At the Guggenheim Museum, the original connection with the Guggenheim family stifled gifts from other potential patrons for some time. For these organizations, donors have considerably more power than the typical small donor at Save the Children or the Girl Scouts.

One substantial donor for many organizations is the government. In 1989, approximately 25% of the revenues of the typical nonprofit in the U.S. was provided by the government.[11] In health, social, and legal services, the contribution of the government is even larger. In these sectors, as Salomon suggests, the government becomes a partner to the nonprofit.[12] As with all partnerships, the result is some loss of control.

Consider the example of arts organizations. Direct federal support of nonprofits arts organizations started with the creation, in 1965, of the National Endowment for the Arts (NEA). In the late 1980s and early 1990s, this partnership faltered, for two reasons. First, the funding levels from NEA dropped precipitously. The 1985 grants for dance, for example, were 22% less than they had been in 1975, despite the considerable increase in inflation during the period.[13] Moreover, some claimed that the agency was exerting considerable pressure on arts organization to alter their mix of activities. Here, we see a clear example of the dangers of concentrated donors.

In most cases, nonprofits have little power relative to the government, but this is not always the case. In particular, in cases in which government agencies are using nonprofits to provide services as substitutes for government activities, those nonprofits can wield considerable power. In this case, the government is a client—not a donor— and may be less powerful. Consider the following quote from the former executive director of Brooklyn's Catholic Charities, Auxiliary Bishop Joseph M. Sullivan:

> We are constantly being asked to take on new projects that no one else will handle—and we've had to learn to refuse some of them. However, when we do take on a new project, we do so on the condition that we receive 100% funding from the governmental agency concerned.

What kind of donor power do we see at the United Way? For the United Way, the corporation that serves as the site for the fund drives and provides corporate sponsorship is the main donor of interest. The power of this group is substantial and, indeed, much of United Way's efforts are directed toward this group. In a 1989 meeting of Connecticut United Way executives, for example, Andrew Sigler, CEO of Champion International, one of the largest manufacturing operations in Connecticut, referred to himself and other CEO's as the "gorillas in the corner," in terms of their power over United Ways; it is an apt metaphor. For individual United Ways, it will be important to understand just which gorillas are about to emerge from the corner.

Supply

On the left of the Six Forces diagram, in box 6, we look at the supply part of the picture. Suppliers can exert bargaining power over an organization by raising their prices, or by reducing the quantity of the good or service supplied. The kinds of questions one would want to ask about suppliers focus on the level of competition in their industry: How many alternative suppliers are there? The more alternatives there are, the less is the power of any one supplier. Does the supplier sell to other markets and, if so, how important are they to the supplier industry as opposed to you? When suppliers sell in a number of different markets, they can often exert more power over any one of those markets. All of these questions go the issue of how much power each supplier has: How important are you to the supplier versus the supplier to you?

The power of the supplier is determined by the concentration of the supplier's industry and the availability of good substitutes.

Who are the typical supplier industries for the nonprofit? In the case of a manufacturing operation, nonprofit or for-profit, the analysis of suppliers typically involves a discussion of other firms. For example, an analysis of General Motors would include, under this box, a discussion of the structure of the auto parts industry. Lack of competition in the auto parts industry would be expected to squeeze profitability from General Motors because auto parts manufacturers could raise their prices to General Motors. We see similar patterns in some nonprofit activities. Understanding the structure of the art market is surely essential to running a museum like the Getty, engaged in an ambitious acquisition program. Similarly, increased concentration in the hospital equipment market would be expected to increase costs for hospitals and thus reduce their profit.

For most nonprofits, a more typical concern on the supply side is changes in the power of the labor force. On average, approximately one half of the operating expenses of the typical charitable organization consists of labor expenses. Moreover, a substantial fraction of the nonprofit is typically professional, and these professionals often wield more power because of their alternative opportunities. An excellent example of this is in the area of teaching. For most elementary schools, private and public, women have historically made up the bulk of the teaching staff. In the 1950s and 1960s, alternative opportunities for these women were relatively modest and, as a consequence, teaching salaries were low, reflecting the low bargaining power of these women. In the 1980s, under pressure from competition for this labor force from other sectors of the economy, teachers' salaries increased rapidly. The consequence has been considerable pressure both on private school tuition levels and on public school budgets.

Return again to the United Way example. Much of the United Way labor force is volunteer, corporate leaders who are responsible for campaigns in their offices. For the United Way, the task is to understand what motivates these volunteers. In the past, at least in some firms, United Way corporate coordinators were almost conscripted by their employers. If United Way's power inside the corporation drops somewhat as new competitors come into the market, the United Way may find itself having to motivate corporate volunteers more.

Industry Structure: Sources of Advantage

Once we have gone through the Six Forces schematic, we should have some sense of the level and character of competition facing the nonprofit both from firms within its own market and from firms in related markets. This analysis will also provide us with some sense of where new axes of cooperation may prove most fruitful.

A second task in deepening our understanding of the market is to take a more microlook inside the industry and seek out the *key success factors* inside that market.

> **The key success factors in an industry are those characteristics that are essential to successful performance in that industry.**

Once we understand the key success factors in an industry, we can use these to develop an inventory of our own organization—for-profit or nonprofit—comparing our own traits with what we believe to be important in the industry. The key to sustained success in a market is clearly to run an organization that is good at all the things that really matter in that industry.

There are a number of techniques that have been developed in the for-

profit world of strategic planning to try to identify the key success factors in a market. We will review the several that seem most helpful in the nonprofit context.

Strategy 1: Survey Expert Opinion Inside and Outside the Organization

The obvious first place to begin in trying to identify those characteristics that are essential to surviving in a market is to survey the views of field experts, both inside and outside the organization. What do the people inside your own organization think is essential? Is there a literature in the field, either academic or business? If so, what does it say?

Some of the information you wish to know will already have come up in a discussion of the entry barriers into your market. By saying that scale economies are an important entry barrier in a market, for example, we are saying that size is a key success factor. If distributional access is an entry barrier, then a good distribution network is clearly critical. And so on. Only some of the key success factors, however, will typically be pinpointed through the competitive analysis. The task now is to refine and supplement this initial list.

In conducting this first survey, it is essential to look at the differences between what insiders and outsiders say. Consider the following several examples. Levi Strauss & Company produces clothes, principally denim jeans. It is a company well known for its progressive labor policy; benefits are good, wages are above industry standards, and lay-offs are rare. If we asked Levi Strauss & Co. executives to give us the key success factors in their market—jeans—many would say a stable labor force. Yet, the nature of production in this industry—uses unskilled labor, repetitive work—indicates that stability in the labor force is not critical to low costs. Most of the firm's rivals do quite well with rather high labor turnover. Levi Strauss, *because it is successful and it has a stable labor force, may believe such a labor force is essential to success.* There is a difference, however, between those traits that a successful firm has and those that are *necessarily needed* to be a success. Only by looking rather broadly at an industry can we begin to identify the latter.

Another example of the kind of perspective generated by comparing inside and outside opinion comes from the educational field. In doing its planning for the future, a middle-sized, private school in the Northeast was trying to decide whether to continue its practice of running for only half day on Wednesday, a common private-school practice. The school addressed the wisdom of this policy by running a survey of its parent body. By and large, the parent body favored the current practice. These parents, however, are certainly not a representative body of potential customers for the school; these people chose the school, *knowing it had a half-day Wednesday policy.* Thus, this group is likely to have a biased view, compared to the general population from which the school might hope to draw future students. This is not to say that current parents ought not to be consulted. The opinions of insiders are critical, but such views need to be weighed along with the views of outsiders as well if an organization is to grow over time.

Strategy 2: Analysis of Market Survivors

In private industry, one way economists use to try to identify key success factors is by examining common characteristics of those firms that have survived in that industry. Thus, one way we might estimate the minimum size needed in an industry (sometimes called the *minimum efficient scale*) is to look at Census data and see what is the minimum size category of firm that has either maintained or increased its share of the market over time. In another area, we might examine whether all of the growing firms in an industry invest heavily in marketing, or research and development. And so on. This approach has been called the *Survivor Technique.*[14] Its usefulness rests heavily on the basic economic proposition that inefficient operations will be weeded out by the rigors of the marketplace. Thus, if a number of firms of a given size survive for a substantial period of time, that size cannot be an inefficient one. If only some organizations advertise their brands, then this is probably not essential to operations. And so on.

I would also argue that in the nonprofit world, over time, inefficient firms are weeded out. This is not to say that all long-lived nonprofits can support themselves; most require infusions from generous donors or government. One of the skills that helps the nonprofit to serve may be its political acumen. Unless these organizations are skilled at raising funds and parsimonious in spending them, however, they will not survive in the long run. Thus, in the nonprofit world as well as in the for-profit world, we can learn much from examining the characteristics of stable firms in a market.

Consider, for example, the market for extracurricular services to disadvantaged children. What are the key success factors in this market? The Boys and Girls Club of America is one example of a stable participant in this market. It is a national organization that works through local affiliates to "provide support for children from disadvantaged circumstances." What can we learn about the market from looking at publicly available data about their operations?

Looking at the Annual Report of the Boys and Girls Club, we see that in 1990, 49% of their budget was spent on salaries, while 1% went to supplies. Even this simple information from the budget suggests that labor relations are likely to be considerably more important in this market than is inventory control. The allowance for depreciation is also rather modest, suggesting that this organization manages its operations without enormous building expense. Indeed, further investigation suggests that many of the programs run by this organization operate through schools, churches and public housing facilities. Again, good staff seems to be key; independent facilities appear not to be. On the revenue side there is also information to be gleaned. We see that just over 50% of the revenues of the Boys and Girls

Club comes from public support, while less than 1% comes from United Way. Here, too, is information about the importance of individual fundraising efforts as opposed to United Way networks.

Ideally, one would want to do this analysis for several years and several different organizations. One would also want to investigate information beyond that contained in the financial reports. Nevertheless, even a cursory review gives us a start on the key success factors and helps us to begin to distinguish idiosyncratic organizational characteristics from key success factors common to a market.

There are several caveats to using either of the two methods described here, surveys of experts or analysis of success stories. Both methods really address the question, What have been the key success factors so far in this market? If the market is rapidly changing, so, too, will the key success factors be changing. Some organizations will be made obsolete; others, with quite different structures and strategies, may come to dominate. Trying to figure out what will succeed in the future is clearly much harder than identifying the commonalities of the past. Second, many organizations—for profit and nonprofit—operate within distinctive niches in an industry, and key success factors may differ substantially across niches. Surviving as a Midwestern military academy may require quite a different set of assets than surviving as a New England Friend's school.

Summary

In this chapter, we have looked at ways in which the market in which nonprofit organizations operate can be analyzed. We focused on the importance of understanding the structure and dynamics of the marketplace and on anticipating the changes that are likely to occur. In a sense, the chapter reflects the recent observation by John Garrison, president of National Easter Seal Society, on the importance of good management: "Commitment isn't enough anymore. You also have to have professionalism or you're going to go out of business."[15] Part of that professionalism involves a deep understanding of the market.