A Grounded / Multi-attribute Utility Theory of Income Portfolios

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Milwaukee, WI
December 7, 2007

Theories of Income Portfolios

- Economic Theory: Nonprofits choose income portfolios that will minimize risk, maximize return
  - ***Systemic risks***: wars, recessions, massive market shifts that have ripple effects
  - ***Non-systemic risks***: change in demand for a particular product, technological development that renders a program obsolete
- Political Theories: Nonprofits pick income portfolios that will maximize their centrality, visibility, and prestige in the community
  - Seek "tipping point" of diverse funding sources
  - Seek highly prestigious grant to increase visibility (e.g., Ford, Kellogg)
- Psycho-social theories: Donors derive various types of "returns" and nonprofits try to position themselves to satisfy multiple donor objectives
- Contingency Theory: Mission is what drives income portfolios

Grounded / Multi-attribute Utility Theory of Income Portfolios

- Income decisions are made not only by “organizations” but also by individual people who have values, objectives, perceptions regarding the income options available to them
- These values, objectives, perceptions may be embedded deep within the actor’s frame of reference
- Qualitative methods derived from “grounded theory” can elicit deeply embedded values (constructs) used by actors to differentiate and rank various income options (descriptive theory)
- Multi-attribute methods can be used to incorporate these judgments into specific contexts and decisions to “optimize” preferences (normative theory)
- Trade-offs are made and different income streams may have vastly different perceived values under different conditions

Many Applications of Grounded Theory, Both Theoretical and Practical

- Family therapy
- Market research
- Political research
- Municipal management and innovation adoption
- Assessment of nonprofit board members
- Interpretations of outcome management schemes used by donors
- Preferences for alternative income streams in a nonprofit portfolio

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Example #1: Income Portfolio of the *Human Services Center Corporation*, Pittsburgh, PA

Gifts from individuals	5%
Gifts from Corporations	8%
Foundation grants	2%
Fees for service (Membership dues and rent)	59%
Government grants or contracts	12%
United Way Allocations	11%
Commercial enterprise	3%

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Strategic Shifts Over 5 Years

- Reduce foundation grants from 16% to 2%
- Reduce United Way from 16% to 11%
- Increase private giving from 5% to 13%
- Increase dues and earned income
- Strategic directions
  - Reduce risk
  - Diversify revenues
  - Build stability and R&D fund (endowment)

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Example #2: Income Portfolio for the Historical Society of Western Pennsylvania

Gifts from individuals	13%
Gifts from Corporations	6.5%
Foundation grants	19%
Fees for service (admission & other fees)	18%
Endowment income	17%
Government grants or contracts	11%
Enterprise	8.5%
Other	7%

Strategic Shifts Over 5 Years

- Relatively few big changes
- Strategic directions
  - Increase stability via government line-item (Goal is 30% of total revenues)
  - Low risk earned income
  - Incremental, not dramatic, change

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A Grounded Theory Exercise

1. United Way Allocation

2. Foundation Grant

3. Special Event Income

In your opinion, how are two of these income sources alike, and different from the third?

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A Grounded Theory Exercise

1. Fee for service
2. Individual donations
3. Government Contract

In your opinion, how are two of these income sources alike, and different from the third?

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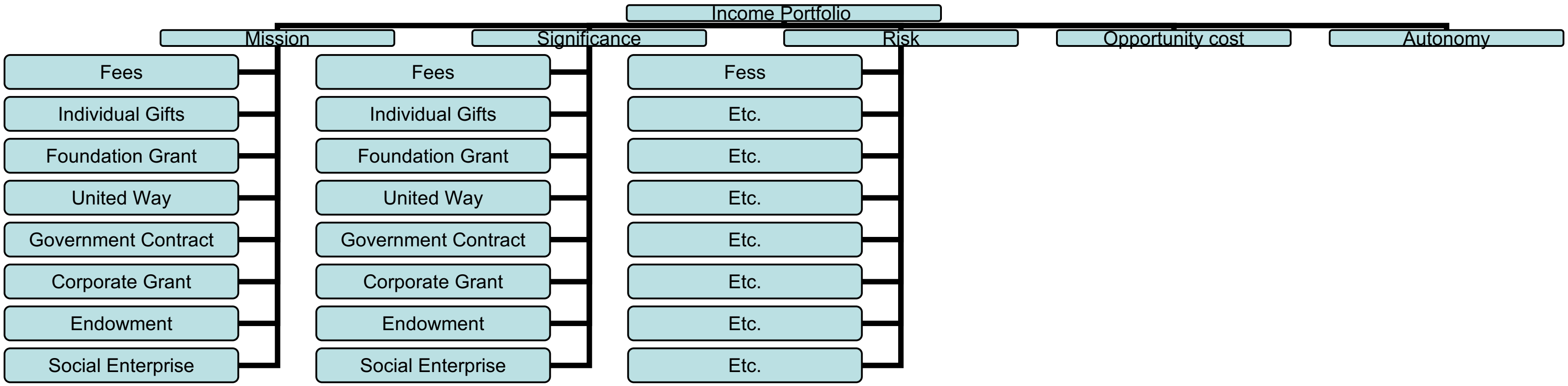
Cedar Hill Community Development Corporation (hypothetical)

- Assume decision makers generate the following criteria for evaluating different income streams:
  - ***Mission appropriateness***: the extent to which the income source is consistent with and supports the mission, values, and philosophies of the organization
  - ***Significance***: the short-term and long-term potential of the income source to generate significant streams of income for the organization or to fill important gaps in the existing income portfolio.
  - ***Risk***: the likelihood that a given income source will yield significantly less than expected over a given period of time.
  - ***Opportunity Costs or Trade-offs***: the prospect that pursuing a given income source will preclude efforts to pursue other income sources
  - ***Autonomy***: the extent to which the income source restricts the independence or autonomy of the organization

From Descriptive Theory to Normative Theory

- Use of Multi-attribute Utility Theory to first rank-order the desirability of the criteria, then order the desirability of various income sources relative to the criteria
- Analytic Hierarchy Process is a good way to do this

Analytic Hierarchy Process



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Assume these are the Perceived Relative Importance of Income Attributes Via AHP

Income Attribute (elicited from decision-makers via repertory grid technique)	Weight (elicited from decision-makers via Analytic Hierarchy Process)
Mission appropriateness	.30
Significance	.30
Risk	.20
Opportunity costs or trade-offs	.10
Autonomy	.10
Total	**1.00**

Hypothetical Mix of Income Sources in the Portfolio

Plausible Income Sources	Desired Relative Percentage of the Income Portfolio (derived via the Analytic Hierarchy Process)
Fees for service	.15
Individual gifts (including annual campaigns, planned giving, etc.)	.05
United Way allocations	.00
Foundation grants	.10
Government grants / contracts	.40
Corporate gifts or grants	.15
Endowment earnings	.05
Social enterprises	.10
Congregational / Denominational Contributions	.00
Special events	.00
Total	**1.00**

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Evaluating Attractiveness and Capacity
Adapted from Hedley (1977)

Attractiveness of Income Source: Neighborhood Grocery Store as a Social Enterprise			
Factor	Weight	Rating of Grocery Store	Score
Mission appropriateness	.30	5	1.50 (.30 x 5)
Significance	.30	5	1.50
Absence of Risk	.20	2	.40
Absence of opportunity costs or trade-offs	.10	2	.20
Threat to autonomy	.10	5	.50
Total Score			**4.10**
Organizational Capacity			
Factor	Weight	Rating of Grocery Store)	Score
Staff and volunteer competence	.50	5	2.50 (.50 x 5)
Infrastructure support	.30	3	.90
Community reputation and image	.10	5	.50
Culture and tradition	.10	5	.50
Total Score			**4.40**

Mapping Components of the Income Portfolio
Source: Adapted from Hedley (1977)

Income source Org. Capacity	**Low Attractiveness**	**Medium Attractiveness**	**High Attractiveness**
Low Capacity	Ignore these income options	Invest in capacity only if there is viable long-term growth potential or sustainability for this income source	Mismatch of capacity to attractiveness. Test, Invest in R&D, and capacity building. Observe others who are further along the lifecycle, mimic their best practices
Medium Capacity	Divest or divert capacity to other income options	Well matched capacity to attractiveness. Focus on sustaining incomes rather than aggressive growth.	Invest (build strength internally) or collaborate (via joint venture, strategic alliance, cause related marketing, etc.)
High Capacity	Mismatch of capacity to attractiveness. Divert skills to more attractive sources if possible	Grocery Store No additional investment in capacity. Sustain or grow these incomes	Aggressive Growth of the Income Source or Protection (Defense) of a "signature" source

Critique of Grounded / Multi-Attribute Utility Theory

- Must take account of history and past decisions
- Must take account of industry standards (institutional theory)
- Must take account of unique local conditions and resources
- Must take account of group process and negotiation

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