

## Crafting a Sustainable Nonprofit Business Model Is it Possible in the Arts & Culture Sector?

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Discussions, articles, and many sleepless nights for board and staff leaders in the arts and culture sector seem to revolve around the concept of developing a sustainable or best business model. This mirrors the issues that all sectors—public, private, and nonprofit—face in meeting the challenges of an ever-changing world. For private and nonprofit firms, some of this dialog comes in the context of the organization’s strategy for achieving operational efficiencies in a way that maximizes impact and revenues while minimizing costs. That sounds simple enough. So why is realizing that sustainability goal so elusive?

Generally speaking, deeper questions quickly surface when institutions discuss their strategy, operations, and business model. These questions tend to be asked separately at different times, but for many organizations they often culminate in a decision to determine what is the best model, which organization has it, and how they can create one.

In their 2010 *Journal of World Business* article, “Sustainability of nonprofit organizations: An empirical investigation,” Jay Weerawardena, Robert E. McDonald, and Gillian Sullivan Mort discovered that nonprofit organizations believe the external context in which they operate is becoming more challenging and competitive. This is leading socially entrepreneurial nonprofits to shift away from basing their strategic and operational decisions solely on past experience, industry norms, and resource dependency. These institutions are focusing on creating innovative business models and practices by shaping their strategic responses with a deeper understanding of the internal and external forces that are impacting their organizations. With this in mind, is there a single sustainable business model in our rapidly changing world?

In this edition of *Arts Insights*, we seek to clarify the difference between strategy, tactics, and business model and to highlight the properties of a sustainable business model. All this may only be the start of an ongoing dialog about the challenges and opportunities ahead for the dynamic nonprofit arts and culture industry.

### **Strategy, Tactics, and Business Model – A Few Definitions**

Before we get to the answer of what the best business model is in the unique nonprofit arts and culture sector—one that relies heavily on the generosity, wisdom, and resources of numerous individuals, businesses, foundations, and government agencies—let us begin by highlighting the three key words/phrases. Organizational strategy, tactics (sometimes referred to as operations), and business model seem to mean different things to various stakeholders. At times, these words are used interchangeably, which can create confusion in the broader discussions around strategy and sustainability.

In the January-February 2011 article in the *Harvard Business Review (HBR)*, “How to Design a Winning Business Model,” Ramon Casadesus-Masanell and Joan E. Ricart shed important light on how to think about strategy as the “primary building block of competitiveness,” arguing that “the quest for sustainable advantage” likely begins with the right business model. For this article, we will continue to use their definitions of our three key terms: strategy “is the plan to create a unique and valuable position involving a distinctive set of activities,” while the business model consists of how an organization “operates and creates and captures value for stakeholders” and tactics are the “residual choices open to a company by virtue of the business model that it employs.” The authors go on to use the analogy that, “strategy is designing and building the car, the business model is the car, and tactics are how you drive the car.”

## Elements of Strategy

Donald C. Hambrick and James W. Fredrickson take on an important question that many organizations face in their article of the same name, "Are you sure you have a strategy?" (The Academy of Management Executive, 19.4, Nov 2005: 51-62). In it, they tackle issues related to strategic fragmentation, catch-all phrases, and statements that companies use as strategies when they are not. As arts and culture leaders, perhaps the most interesting point the authors make is that strategy, derived from the Greek, *strategos*, means "the art of the general." It is perhaps impossible to segment or isolate specific elements of a strategy without looking at their synergistic whole. These elements include:

**Arenas:** Where will an organization be active? In the culture sector, this can take many shapes and forms both inside and outside their facilities: in electronic or social media, on the internet, and well beyond.

**Vehicles:** How will it get into those arenas? This may include collaborations, new program development, and any number of paths to reach the broader audience.

**Differentiators:** How will we gain participation and support for our programs and services by highlighting our value proposition and positive institutional impacts?

**Staging:** What will be the speed and sequence of the moves that the organization will make?

**Economic logic:** How will the organization obtain its (financial, social, cultural, community, and/or other) returns in its quest to achieve sustainability?

At times there are key stakeholders with invaluable for-profit business savvy who believe that operational efficiency is the strategy of running the nonprofit more like a business with the financial bottom line as the primary goal. At the same time, experienced nonprofit sector professionals may understand that the larger mission and intended institutional impacts – the building blocks of the strategy – are constrained by lack of resources, all of which influence the business model. A blur of daily operations, activities, phone calls, and meetings can complicate these perspectives, creating an illusion that addressing short-term or urgent needs is the path toward achieving both the strategy and the underlying business model. Such fragmentation does not advance the concept of what is inherently long-term sustainability. Looking at each of the five elements above, however, and then integrating them into a cohesive strategy, will allow for risk reduction in selecting a business model that is most effective.

## Policies, Assets, and Governance – Choices and Consequences

As Casadesus-Masanell and Ricart point out in their *HBR* article, organizations generally make choices in three key areas – policy, asset, and governance – when crafting their business models. Importantly, they find that these choices can have flexible or rigid consequences. Discounted ticket or admission pricing, for example, is flexible and could result in higher sales, while operating in resource scarcity mode for extended periods of time can become part of a rigid and embedded organizational culture. Many organizations have seen the latter consequence result in detrimental policies that seek to restrict otherwise unrestricted bequests or large contributions into the (permanently restricted) endowment (asset). At times this is simply the result of confusion that still exists about the definition of endowment versus the comingling of unrestricted, temporarily restricted, and permanently restricted funds into a single account in an effort to maximize returns on those investments. In other instances, however, the policy creates a lean but inefficient business model that lacks the financial resources it needs to operate, achieve its strategic initiatives, and create long-term sustainability. Perhaps an analogy would be setting up a family's college trust fund but not releasing enough monies for the first child to attend because returns on the investment need to be maximized for the last child to attend. In arts and cultural organizations with endowments, these funds are typically held in trust to protect its long-term legacy. But if the organization cannot survive short-term economic jolts, the restrictions can become an impediment through a rigid policy (choice) that creates negative results (consequences).

Choices and consequences in the nonprofit sector are perhaps even more pronounced and complex than in for-profits. Individuals in governance and policy roles, such as board members, can also provide an organization or otherwise connect it to important financial, human, technological, or other assets. Additionally, many of these key individuals in the arts and culture sector are also consumers of the product or service offered by the organization for which they are setting policy and providing governance. Board members of international pharmaceutical companies, for example, may never use the drugs developed for patients, whereas cultural institution trustees likely will immediately see the consequences of their choices. Running it like a business takes on entirely new meaning and creates far more intricate challenges for nonprofits when it comes to strategy, tactics, and the business model in this situation.

## A Good Business Model: Are We There Yet?

Ultimately, the business model addresses who the customers are, what they value, and how the organization delivers value to them (Peter Drucker, *HBR* September-October 1994, “The Theory of the Business”). If strategy is about designing and building our cultural institutions and tactics relate to how they operate, perhaps the institution as “the car” is the most elusive analogy of the three to solidify. Casadesus-Masanell and Ricart ask questions that point to three characteristics of a good business model highlighted here. Is the business model:

1. Aligned with the mission and goals of the organization? Ultimately, does the business model enable building momentum towards the one or more goals (financial, cultural, community, social, educational) established as part of the strategy?
2. Self-reinforcing? As an example, if a theater company believes its purpose is to provide low-cost access to its programs for those in socioeconomically disadvantaged communities but a majority of its seats are tailored to those with the means to pay, is the business model structured correctly?
3. Robust? Can your organization capitalize on its strengths and opportunities while minimizing its weaknesses and threats (SWOT)? Pankaj Shemawat asks in his 1991 book *Commitment: The Dynamic of Strategy* and subsequent articles, if the business model can fend off four key challenges – imitation (direct/indirect competitors), holdup (customers/suppliers bargaining), slack (organizational complacency), and substitution (new products/services).

With that the above in mind, organizations must consistently review various internal and external forces, their SWOT, available resources, industry changes, and quality of its programs and services. Ultimately, how effectively and consistently is the cultural institution delivering on its promises to the community and wide-ranging stakeholders that it serves?

## Strategic Planning and Implementation Challenges

The Academy of Management, one of the leading associations of scholars dedicated to creating and disseminating knowledge about management and organizations, has 25 disciplines represented by various divisions and interest groups. Interestingly, one of the newest of these is Strategizing Activities and Practice (SAP), whose approach to scholarship and teaching ultimately states that, “strategy is not something that firms have, but something that people do” (Johnson et al. 2003; Jarzabkowski et al. 2007). Perhaps this is a further testament to the complexities of strategy, tactics, and business models that constantly require careful quantitative and/or qualitative research and different ways of thinking, learning, and doing business.

Creating a meaningful strategy in the nonprofit arts and culture sector that has both an innovative business model and effective tactical operations has never been easy. Scholars and practitioners—private, public, nonprofit, and any combination of these—struggle to comprehend the depth and breadth of issues that any business faces. All firms hope to advance sustainability by having an appropriate strategy, effective tactics, and the right business model. Through research, trial and error, and pure passion about their respective missions, cultural organizations have learned a tremendous amount about strategic frameworks, analytical tools, and organizational efficiencies. Congratulations! This was no easy task but the work must continue if these community pillars hope to survive and thrive.

## Conclusion

A solid understanding of the dynamics within, across, and surrounding the nonprofit arts and culture sector will be key to its future success. The industry, institutions, and communities in which they operate are ever-changing. With both live and online competition in the arts and entertainment world, competition will become more intense and sustainability more problematic as resources shift and audience options increase. Focused strategies, efficient tactics, and well-defined business models must evolve, as sustainable organizations will need to quickly adapt as they seek to learn from their past experiences, live in the dynamic present, and look to an uncertain future simultaneously. Through the ages, extremely committed stakeholders have left a tremendous legacy for the advancement of arts and culture as a cornerstone of resilient communities. Fortunately, their connection, capacity, and commitment will bode well for cultural organizations that seek to realize impactful strategies and sustainable business models.

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### Dr. Bruce D. Thibodeau, President

Dr. Bruce D. Thibodeau founded ACG in 1997 and, as its President, has been embedded in numerous projects in all practice areas to grow institutional sustainability, advance the arts and culture sector, and enhance communities served by this vibrant industry. He has guided hundreds of clients in achieving effective leadership transitions, planning cultural facilities, increasing revenues, developing dynamic institutional brands and messages, crafting strategic plans and business models, and revitalizing board governance practices. Prior to founding ACG, Dr. Thibodeau held various management roles at the Los Angeles Chamber Orchestra, Boston Symphony Orchestra, Hartford Symphony Orchestra, Santa Fe Chamber Music Festival, and Museum of Contemporary Art Los Angeles. Dr. Thibodeau has conducted extensive research in a threefold exploration of stakeholders, nonprofit arts management, and cultural facility project management to highlight how stakeholders influence, and are influenced by, the activities and practices

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**Contact ACG for more information on how we can help your organization clarify its strategy, craft its business model, and improve operational efficiencies.**

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