

The Shifting Boundaries of the Mixed Economy and The Future of the Nonprofit Sector^{1[1]}

by

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Abstract

The nonprofit sector exists because it can solve better than for-profit firms problems associated with the provision of products with publicness (nonrivalry or nonexcludability) attributes, or those affected by asymmetric information between providers and customers. This advantage is likely to be eroded in the future by various technological advances, particularly in the area of information transmission, analysis, storage and retrieval, and by the increase in the effective size of markets. Consequently, the demand for nonprofit organizations will possibly decline in the future. On the other hand, the operational efficiency of nonprofit organizations is likely to improve due to possibilities of stricter audit of and control over management made possible by enhanced access by nonprofit stakeholders to budgetary and operational information. This will help nonprofit organizations respond better to various failures of for-profit firms and to the insufficiency of government correctives. It is difficult to forecast the net effect of the myriad factors that work in opposite directions on the demand for and supply of nonprofit organizations, although it appears to this author that the economic weight of nonprofit organizations and their distinctive features will wane.

I. Introduction

A substantial transformation has been taking place in the world economic order. Dramatic changes are everywhere: the diminution of government ownership of industry and services, the reduction in the role of manufacturing in favor of diverse services, the technological revolution pervading most aspects of life, an increase in the wealth of some segments of many societies and a concomitant rise in inequality, and the globalization of economic affairs with the accompanying decline in the role of national economies and politics.

How is this transformation likely to affect the organizational makeup of the economy? The three principal forms of economic organization and ownership – the for-profit, government, and nonprofit organizations – operate in economic niches where they enjoy some comparative advantage arising from their respective principles of operation. The strength of the comparative advantage of each organizational form depends on various factors, such as the extent to which they can respond to consumer and donor demand, the ease with which shareholders and other stakeholders can articulate their interests with respect to hired managers, and their operational efficiency and law that support it. Changes in these factors affect the relative advantage of the three principal forms of organization and therefore change the organizational makeup of the economy.

How do changes in technology, the economy, globalization and other areas affect the boundaries that separate the for-profit, government, and nonprofit sectors? What lies ahead for the nonprofit sector in the foreseeable future? Will there be a sustained need for its particular services? Will it be able to satisfy needs that are not met sufficiently well by the for-profit sector and by government?

To investigate these issues, I examine first what constitutes the comparative advantage of nonprofit organizations relative to government organizations and particularly to for-profit firms. I argue in section II that nonprofit organizations have an advantage over for-profit firms in the provision of products that have significant elements of ‘public goods’ – substantial nonrivalry in consumption and difficulty in charging consumers an economically appropriate price for their consumption – and when consumers have an informational disadvantage relative to sellers concerning the value,

usefulness, or quality of the products they purchase. Nonprofit organizations have a particular advantage in the provision of ‘relational goods,’ which can be provided only by those who participate in the social or emotional production process itself. On the other hand, nonprofit organizations have significant disadvantages with respect to their ability to engender entrepreneurship, obtain financing and conduct efficient operations, although they enjoy the dedication of some of their employees, consumers and donors.

Second, I assess the effect of technological, economic, social and political changes on nonprofit organizations’ comparative advantage. The vast improvements in information technology, I argue in section III, are reducing the informational advantage of nonprofit organizations, as well as making it easier for for-profit firms to provide products with public good aspects, to the effect of weakening nonprofit organizations’ comparative advantage. The increase in the size of markets that accompanies globalization accentuates this trend. The weakening of social bonds and the diminution of various forms of social capital make it more difficult for nonprofit organizations to enlist entrepreneurial effort and to ensure participation in the organizations’ affairs. Technology will likely have a favorable effect on various stakeholders’ ability to audit and control nonprofit organizations in which they have an interest, and thus improve the efficiency of their operations and strengthen them. On balance, my judgment is that the place of nonprofit organizations in the economy will likely to weaken in the foreseeable future.

I conclude the essay in section IV with brief conclusions regarding the future of the nonprofit sector, and with policy ideas aimed at preserving the place of nonprofit organizations in the economy. Predicting the future is not a common theme of academic articles. This final section highlights the speculative nature of the enterprise undertaken in this essay.^{2[2]}

^{2[2]} A brief statement of the main points made in this article can be found in Ben-Ner and Tradewell (2001). The article is written from the perspective of an economist but is intended for an audience that includes other social scientists. Many of the arguments and claims summarized here are developed more fully in my work as cited in the references; my own work is an extension of the pioneering contributions of Hansmann (e.g., 1980) and Weisbrod (e.g., 1988). The essay largely ignores the labor market, and speculates very little on how governments may change their behavior in the future.

II. Why is there a mixed economy?

The heterogeneity of organizational forms is directly related to heterogeneity in the demand for key attributes of products, whether goods or services.^{3[3]} Differences in attributes stem, in turn, from differences in the production, delivery and consumption of products. In this section, I develop the following argument: the for-profit firm is the most effective and efficient form of organization in the production, delivery and consumption of purely private products (products that are both rival and excludable), and of products that are purchased under conditions of complete symmetry of information between producers and consumers, but government and nonprofit organizations have important advantages in the provision of products with some public elements and products provided under conditions of asymmetric information between providers and customers.^{4[4]}

However, both nonprofit organizations and government organizations suffer from disadvantages in their ability to raise capital, in their motivation to be entrepreneurial, and in the ability of their stakeholders to exercise control over management. These disadvantages constitute barriers to entry for nonprofit and government organizations. Hence, nonprofit and government organizations will prosper only when their advantages in the production and delivery of public products, and products afflicted with asymmetric information, are large enough to overcome these barriers.

A. Rivalry and excludability vs. nonrivalry and nonexcludability of products

Purely private products are those goods and services which (1) are produced and consumed in a way that the units that one consumer uses cannot be used by another consumer (*rivalry*), and (2) each consumer can be charged for each and every unit of his or her consumption (*excludability*). In contrast, purely public products are both nonrival and nonexcludable in that they can be used by any number of consumers without degradation of the quantity or quality of the product they each consume, and individual

^{3[3]} I use the term product to designate both goods and services, and therefore refer to economists' public goods as public products.

^{4[4]} The term 'customer' refers to both consumers and donors. The purpose of this section is to clarify the circumstances that favor the existence of nonprofit organizations in a market economy, and the tradeoffs between nonprofit and government provision are considered here only tangentially (for a detailed examination of these issues see Weisbrod, 1988 and Young, 2000).

consumers cannot be charged for their consumption. Both of these attributes are continuous, so that a product may be characterized by more or less rivalry and excludability. Although some products combine extreme degrees of the two attributes, many products exhibit different degrees of the two. Moreover, these attributes are not fixed but are variable to some degree; for example, excludability depends on the cost of exclusion, so that a purely private product entails, by definition, zero cost of exclusion and a purely public product entails an infinite cost of exclusion.^{5[5]}

Consider a few examples. A can of soda is rival because what one person drinks cannot be enjoyed directly by another person, and is excludable because consumption can be limited to those who pay (if fairly simple rules of ownership exist and are easily enforced so that exclusion costs born by vendors are very low). A can of soda may therefore be regarded as an almost pure private product. In contrast, a cup of water from an ocean is nonrival, because even if all the people in the entire world would dip cups in the ocean, the water level will remain essentially unaffected. Access to oceans can be controlled, although probably at very high costs, so ocean water is excludable only to a very limited degree. Ocean water is thus close to the public product end of the spectrum.^{6[6]} The production and consumption of movies concerns the making of a 'master' copy, which entails a large cost, but from which inexpensive copies can be made and screened in different places without any rivalry.^{7[7]} While nonrival, both steps are obviously excludable.^{8[8]}

Consider next the more abstract case of the quality, color, durability and other characteristics of products. The quality, for example, of a certain product is the same for all consumers of the product, and is therefore nonrival. But if the product is available in many variants, each with different quality, then the nonrivalry of the product wanes. The

^{5[5]} The realism of either zero or infinite costs of exclusion is, of course, questionable.

^{6[6]} National defense is a standard textbook example of pure public goods. But national defense is partly rival, because military forces may be active only in one place at a time (this is why, other things being equal, larger countries have larger armed forces). Defense services may, of course, be excludable, as the example of private armies and militias suggests.

^{7[7]} This is true also of many manufactured goods, which involve the production of an expensive 'mold' from which individual units are produced at some additional (marginal) cost.

^{8[8]} The case of television productions is somewhat different: the marginal cost of beaming a movie via TV into an *additional* home is essentially zero in a given broadcasting area, hence this aspect of movie consumption is nonrival, and consumption is nonexcludable in the case of broadcast TV, but excludable in the case of cable TV.

nonrivalry of the characteristics of automobiles produced a century ago was substantial: the black Model T met the demand of the average consumer, and the other (few) consumers who could afford a car had to choose between that model or go without an automobile altogether.^{9[9]} Today, with huge markets for automobiles and technologies that allow rapid adaptation of production lines, automobile characteristics are essentially rival.^{10[10]} Related examples can be drawn from theater, day care for young children, education, health care services, museums, and so on. In small markets, the number of variants – different theatrical productions, or different types of care for children – are limited. Additional examples can be found in the first four columns of [Diagram 1](#).

In the case of rival products each consumer gets something different, matching his or her specific demand. In contrast, with nonrival products all consumers get the same characteristics, hence consumers with high demand will get less of the characteristics they want and consumers with low demand will get more than they want, given the price of the product. The problem with nonrivalry is then that high-demand consumers may have excess demand, and therefore they will be dissatisfied, and in the extreme may not purchase the product at all. If the product is excludable, then each consumer is forced to pay for his or her consumption, generating revenue for the producer. The problem with nonexcludable products is that the provider cannot charge for the product, so under normal market circumstances, the product cannot be provided. These problems diminish as a product moves along the spectrum from nonrivalry to rivalry and from nonexcludability to excludability.

B. Symmetry vs. asymmetry of information regarding products

Symmetry of information about a product is said to exist when both the organization and its customers have free access to the same information about product characteristics and to other matters of interest to customers. Frequently, the producing or the selling organization knows more about the relevant issues than does the customer. The information may regard the durability of a manufactured good, the curative value of a medical drug or treatment, the nutritional content of a food item, the growing method of

^{9[9]} This example is not strictly accurate, since there were a few other producers of cars.

^{10[10]} The characteristics of a *variant* of a product are nonrival to those who consume that variant. But the characteristics of the *product* are increasingly rival as the number of variants increases.

vegetables, the way young children or aged parents are cared for in an institution, how funds collected for improving the living conditions of the poor are actually spent, and so on. The last two columns of [Diagram 1](#) provide a few examples.

The problem with asymmetric information is that it affords the producer or seller the opportunity to take advantage of the relative ignorance of the consumer in order to enhance its profits.^{11[11]} This situation foments suspicion on the part of consumers, and may restrict the size of the market and, in the extreme, eliminate it altogether.

The three attributes of products come together in one type of products, the so-called ‘relational goods’ (Gui, 1996, Gui 2000, and Ben-Ner and Gui, forthcoming). These ‘products’ include the pleasure of exchanging feelings and ideas with other people, the desire to receive the attention of others, the quest for ongoing relationships and for belonging to a group and community. Relational goods are produced directly in social clubs and associations, and more often as a by-product of other activities in both for-profit firms and nonprofit organizations, although nonprofit organizations often tolerate or even encourage the production of relational goods (either because of unmitigated agency problems or because this may be part of the mission of the organization), and they attract as members, workers and volunteers people who care about such goods more than others.

C. The comparative advantage of different types of organization

How can products that are afflicted by substantial asymmetric information concerning characteristics that matter to consumers be transacted on the market? And how can products that are significantly nonexcludable or nonrival be sold on markets such that enough revenue is generated to support production and distribution? This section offers a brief comparative analysis of the responses of for-profit firms and nonprofit organizations to problems associated with asymmetric information, nonexcludability, and nonrivalry, outlining the conditions that lead to comparative advantage of one type of organization over the other.

^{11[11]} Examples of this abound, from peddlers of snake oil to cure various diseases, to selling adulterated flour in 19th century England, to painting over cracks in houses or damages in used cars, to the ordering of unnecessary medical care in contemporary health care institutions.

Asymmetric information

The fundamental problem with asymmetric information is this: the buyer cannot tell exactly what he is getting for his money, and therefore he will part from it only if he trusts that the seller will not take advantage of him, or if the risk of an undesirable outcome is low relative to his best alternative, so that the expected benefit from the transaction is positive. Under what circumstances would the buyer trust the for-profit seller?^{12[12]}

A seller can be trusted if she is a member of the community and is not expected to do anything unfair against her community. This sort of trust may operate in relatively small, stable and homogeneous societies where there are few cleavages that make people readily willing to take advantage of others. In this sort of an environment for-profit firms can prosper even in markets with severe asymmetric information.

A seller can also be trusted if she is known to possess ‘good character’ and risks losing her reputation by exploiting her informational advantage over consumers. For such a mechanism to operate it is necessary that consumers have a collective memory of sorts, whereby knowledge about the behavior of sellers can be generated, collected, stored and transmitted as needed. Such a mechanism can be created and maintained if sellers are known (because they maintain their identity over time, are large enough to attract attention, etc.), if social networks are stable and efficient in processing information, or if there are technological or other means of storing and transmitting relevant information.

The legendary oriental market, the *souk*, illustrates some of the key points raised here. For the tourist, the *souk* is comprised of sellers who are not distinguishable one from the other, stocked with unfamiliar products that cannot be evaluated on the spot for price, quality, durability or even functionality, and where there are no warranties or reputation. Hence the *souk* presents the tourist with a lot of asymmetric information problems. In contrast, for people in the community where the *souk* is located the sellers are identifiable, there is awareness of reputations that are built and maintained over a very long time, and there is familiarity with the products, so the information may be entirely symmetric. What for the tourist is an economically hazardous interaction with an

^{12[12]} There are more aspects to the issue of trust that can be discussed in this essay. For an extensive discussion of trusting and trustworthiness, including references to the literature, see Ben-Ner and Putterman (2001).

untrustworthy seller, for the local consumer this is a secure exchange in which the for-profit firm (the local seller) works just fine. Under these circumstances tourists will make fewer purchases than they would in a more trusting situation.

It is in the interest of both consumers and sellers to develop measures that will allow the operation of efficient markets for products sold under asymmetric information. Such measures will be aimed at improving the trust consumers place in sellers, or directly improving the information available to consumers. In either case consumers will be willing to purchase more of the product in question, and will be willing to pay a higher price than if they suspected that the product is less valuable because the seller is exploiting asymmetric information. There are many corrective measures that improve trust or the quality of information; these measures may be the result of intentional action or the by-product of another action or situation.

One corrective measure consists of government regulation, such as information disclosure requirements (e.g., disclosure agreements in financial markets and listing of ingredients in food products), drug testing, and licensing of child-care institutions. Government regulation is usually restricted to large markets and to products that affect many consumers, and is limited by the government's willingness to act. In many countries, government regulation does not eliminate the problems created by asymmetric information in a range of products and situations.

Another corrective measure consists of voluntary action by firms. Organizations set up by firms with the objective monitoring the behavior of businesses (e.g., the Better Business Bureau in the US), and voluntarily-issued, company-backed and legally-binding warranties, are key examples of what companies do to resolve the problem of asymmetric information. These measures work well in many situations, but are less effective in cases where some firms choose not to participate or have opportunity to renege on obligations they took upon themselves. In addition, the issue of self-regulation may itself be fraught with asymmetric information problems about its value, meaning, and remedies to consumers. Building and maintaining a reputation is yet another important corrective measure, already discussed above. Each of these corrective measures requires an effective legal framework and enforcement.

An entirely different approach to solving the problem of trust entails eliminating the seller's profit-seeking. But elimination of the profit motive does not ensure that the seller will lose the motivation to take advantage of consumers' informational disadvantage. The seller may have a variety of non-profit objectives that can be advanced by exploiting consumers' informational disadvantage. For example, management may want to run a large organization, or support certain causes that contributors do not favor as much as other causes; management can pursue its goals by taking advantage of customers' relative ignorance. Nonprofit organizations are required by law not to pursue profits, but the law does not stipulate specifically what they *must* pursue. Thus, even if consumers believe that the law is enforced strictly, they still have reason to believe that the goals the nonprofit organization is pursuing are not fully consonant with their interests.

A *bona fide* nonprofit organization may therefore pursue objectives that generate a type of product with which the consumer will not be happier than with the adulterated product generated by a for-profit firm that exploits its informational advantage. Consumers can trust that the nonprofit organizational form is a superior alternative to the for-profit firm only if the organization pursues *their* objectives. This will generally happen when consumers have the ability to set the objectives for the nonprofit organization in which they have an interest, and have the ability to oversee it to ensure that it operates efficiently. *Consumer control* is therefore the guarantor of satisfaction of consumer demand; where consumer control fails, the conditions for overcoming the problems with for-profit provision of products under asymmetric information also fail (Ben-Ner, 1987).^{13[13]} ^{14[14]}

Nonrivalry and nonexcludability

The problem with nonrival products is that all customers of a firm are forced to consume the same characteristics and pay the same price, and furthermore, there are no

^{13[13]} See also Handy (1997). Sokolowski (2000) finds empirical evidence in support of the hypothesis that risk and asymmetric information are associated with reliance on nonprofit organizations.

^{14[14]} A nearly identical analysis applies to government organizations. In places where the government's reputation is tainted (e.g., because of political corruption), its ability to produce and deliver credibly under asymmetric information is naturally in doubt. As noted earlier in the context of government regulation, there are various constraints on the extent of government involvement in the market, particularly when it comes to production and ownership.

competing firms that provide variants of the product to satisfy different demands. The price that the firm sets must be low enough to attract low-demand consumers. If high-demand consumers are not numerous enough to pay for the kind of product they like, then they will have excess demand and will be dissatisfied with product. The problem with nonexcludable products is that the provider cannot charge for its product, and hence under normal market circumstances, the product cannot be provided at all.^{15[15]} Thus in the case of nonrivalry and nonexcludability (and of course when both are present, in public products) for-profit firms cannot charge the price that is required to satisfy the demand. As a result, there will be insufficient production of some products. Government provision could deal with the two problems through compulsory taxation, but if (for familiar reasons) government provision is insufficient, some consumers will remain dissatisfied with the level and quality of provision.

To improve provision, dissatisfied consumers or their sponsors (donors) will have to reveal their demand to the provider so that it can charge different prices from them as well as pay a higher price that reflects their demand. But a for-profit firm will generally find it impossible to attract voluntary contributions – the difference between the price that high-demand customers should pay to support the kind of product they want and the prevailing price. The reason is that no individual consumer has an incentive to make contributions but would rather enjoy the fruits of other consumers' contributions. Even the charitable consumers will likely refrain from making contributions to a for-profit firm because they will not trust that the money will be used towards improved provision of the product.

The alternative is to write contracts with individual consumers and donors, or with an organization that represents them, specifying the price, quality, quantity and other characteristics of the product. Individual customers will in general be unable to engage in complex contract writing and enforcement. Large or organized consumers and donors could engage in such contracting, as is often the case between suppliers and purchasers (typically for-profit firms themselves) when price discrimination of the sort discussed here is mutually beneficial.

^{15[15]} With partially nonexcludable products the situation is less severe, and the problem of under-provision will be more moderate. The same holds true of products whose nonrivalry is limited to less important product characteristics.

But in many other instances if customers can organize for the purposes of contracting, they may find it more expeditious to alter the governance structure of their relationship with suppliers one step further, by assuming control over the supplier and requiring it to act fully on their behalf as a nonprofit organization. The resulting arrangement is a nonprofit organization controlled by some customers. The nonprofit organization controlled by customers provides a safe and trustworthy place where customers can reveal their desires (demand) for the product and make donations to ensure that the product (day care for their children, aid to the poor in distant locations, interesting theater productions, etc.) is made available in the way they desire. In order to ensure that the organization is run efficiently, customers must also impose an appropriate governance structure on the organization.

D. Differences in the costs of entry and operation of different types of organization

Nonprofit organizations controlled by their customers have advantages over for-profit firms in the provision of products affected by significant degrees of nonrivalry, nonexcludability, and asymmetric information, and in the provision of relational goods. Nonprofit organizations also have some operational advantages in comparison to for-profit firms thanks to the fact that the tax laws of many countries favor their accumulation of retained earnings. They also often enjoy a particular relationship with their customers through associations, churches and social movements; this offers nonprofit organizations a relatively steady and reliable demand. Many nonprofit organizations benefit from the work of employees and managers who identify with the goals of their organizations and do not require as strong and expensive incentives as individuals working in a for-profit firm.

However, nonprofit organizations often face problems with regard to their internal organization, entrepreneurship, access to capital, accountability, and more generally, with ownership and control. These problems pose obstacles to the efficient operation of nonprofit organizations, so that they may not be the provider of choice even in instances where for-profit or government provision is deficient. To understand the source of these problems, let us consider briefly the requirements for the establishment and operation of an organization.

The first requirement for the establishment of an organization is the availability of entrepreneurial initiative. A nonprofit organization cannot attract entrepreneurs who seek profits. The initiative must therefore come from charitable entrepreneurs, or individuals with demand for the nonprofit form of organization. The second requirement for the emergence of an organization is the availability of funding, which again must come from either those with demand for the organization, or those who care about them. Third, production of products with significant nonrivalry and nonexcludability attributes must be funded not only through the ordinary sale of goods and services on the market, but also through additional voluntary contributions. Fourth, the organization must be able to commit credibly to its customers to maintain its form as an alternative to the for-profit type of organization, in order to retain their support. Finally, the survival of an organization is predicated on its ability to produce efficiently; at the very least, the organization's efficiency disadvantage must not exceed whatever other advantages it enjoys relative to other firms.^{16[16]}

These requirements determine the likelihood of the existence – that is, the supply – of a nonprofit organization. Each of these depends on successful collective action, and is vulnerable to *free-ridership or social loafing* exactly by the very individuals who desire the existence of the nonprofit organization. Individuals may benefit from most aspects of the operation of a nonprofit organization while expecting others to bear the costs of entrepreneurship, of funding the establishment of the organization, of revealing their true demand for the organization's products, of making voluntary contributions, and of controlling management to ensure both the pursuit of the organization's objectives and its efficient operation. Free-ridership may be limited if members of the group can apply social pressure or impose costs on free riders. They can do so if they are part of a cohesive group or a community that can enforce individual behavior in the interests of the group. An important factor that aids nonprofit organizations is the existence of a large endowment of "social capital," a dense network of relations based on mutual acquaintance, trust, and ongoing cooperation that facilitates joint action (Coleman, 1990). However, absent strict control by affiliated organizations or associations that demand accountability from nonprofit

^{16[16]} Cafferata (1997) refers to similar requirements as allocative efficiency of economic policy and efficiency of internal control.

organizations, the governance problem in nonprofit organizations is likely to be more severe than in for-profit firms, and as a result, nonprofit organizations will face greater obstacles to their existence.^{17[17]}

E. The distribution of economic activities across the three sectors

The organization that handles better problems associated with asymmetric information, nonrivalry, and nonexcludability, as well as in the provision of relational goods, will be favored by consumers who believe that they are getting a better deal from it than from alternative sources.^{18[18]} The demand for the products of an organization that is related to the organization's generic ability to handle problems associated with product attributes is effectively a *demand for the type of organization*. The costs associated with the founding and ongoing operation of a particular define the *supply of types of organization*. The general conditions for demand and supply for the nonprofit type of organization relative to the for-profit firm that were discussed in the previous section are summarized in [Diagram 2](#).

The next step in the analysis is to use the results that were derived thus far in order to characterize the distribution of economic activities across the three sectors. There are two central questions: Why is there a tendency for types of organization to concentrate in the provision of certain products? Why are some products provided by more than one type of organization?^{19[19]}

Consider a completely rival and excludable product that is affected by asymmetric information. Let us assume for the sake of the argument that two nearly-identical organizations are standing ready to provide this product. The only difference between the organizations is that one is run for profit and the other not for profit, but otherwise their operations, including efficiency, are identical. Which organization will provide this product? Even with a very limited degree of asymmetric information, the nonprofit

^{17[17]} This issue is examined from a principal-agent theoretic perspective in Ben-Ner, Montias and Neuberger (1993), and applied to governance in nonprofit organizations in Ben-Ner (1994). For a related perspective, see Manne (1999).

^{18[18]} Some consumers may recognize that their preference for an organization is associated with the *type* of that organization, whether for-profit, government or nonprofit. Such consumers may generalize their experiences and in certain circumstances favor particular types of organization.

^{19[19]} See Anheier (1993), Ben-Ner and Van Hoomissen (1993), Borzaga (1993) and Marcuello (1998) for data and analysis that support the premises of these questions, as well as for answers to them.

organization will satisfy the entire demand. Assume now that a product is entirely rival and excludable and that there is no asymmetric information in provision to consumers, but the organizational supply side is slightly favorable to the for-profit firm. Then the only provider will be the for-profit firm, with nothing left for the nonprofit organization, which will have no customers because the price it charges will be higher than the price charged by the for-profit firm. These simple examples suggest the existence of circumstances that can lead to the domination of a product market by one type of organization.

The foregoing discussion assumed implicitly that all consumers in the market are identical in all respects except for their demands. But consumers often differ in their treatment of information, and their ability to act collectively. First, some consumers may be more able than others to overcome informational differences than other consumers. The better-informed consumers will have less need for nonprofit organizations, so there will be two types of organization in the market (ignoring government) providing the same product, one catering to the better informed and the other to the less informed. Second, some consumers may not be as sensitive to asymmetric information problems as other consumers may be, and will choose the provider of a product irrespective of the type of organization. Third, supply-side differences may exist among communities or groups of consumers. Some may be more apt, for instance, to generate initiative and control to help themselves with the founding and operation of nonprofit organizations, and these communities will have a relatively high density of nonprofit organizations relative to others.^{20[20]}

We are now ready for a discussion of changes that can generate changes in the distribution of economic activity among the three sectors.

^{20[20]} Putnam (1993) emphasizes this sort of differences between different regions of Italy.

III. The effects of technological and economic changes on the distribution of economic activity across sectors

The last decade and a half has been a period of substantial change. The change, which has gathered pace since the late 1990s, encompasses most facets of life, from technology to globalization of economic activity, to values, culture, and politics. In this section I use the theory developed earlier in the essay to evaluate how technological, economic, and other changes are likely to influence (1) the prevalence of nonrivalry, nonexcludability, and information asymmetry, (2) the ability of nonprofit organizations and for-profit firms to deal with problems that arise from these attributes, (3) the distribution of products with various combinations of these attributes, and (4) the relative costs of establishment and operation of nonprofit organizations.^{21[21]} This will be followed by an attempt to gauge the *net* effect of the various changes on the nonprofit sector.

A technological revolution is sweeping the world. Despite the fact that the pace with which the revolution is advancing is geographically very uneven, the ever-declining price of new innovations and the rapid transmission of technological developments around the world make it likely that current trends in the United States and other developed nations will eventually transfer to other countries. Technology has many dimensions and manifestations; most of the relevant dimensions are related to developments in the storage capacity, computational ability, and speed of transmission of microchips, as well as the sophistication of the software that runs them. Microchips herald revolutionary changes not only in information-related areas, but also in the use of robotics in production and the introduction of miniature devices, and in consumption in the household and elsewhere. Since technology has so many facets and affects so many areas of economic life, the discussion in this section is dominated by an examination of technology's effects on various issues, particularly those related to information.^{22[22]}

A. Information collection, transmission, retrieval and analysis, and communication

^{21[21]} This analysis of change is an informal application of what economists call 'comparative statics.'

^{22[22]} For background analysis that lends support to the analysis in this essay, see Litan and Rivlin (2001a and b).

The demand side: the waning of nonrivalry, nonexcludability, and asymmetric information

It is worth restating the well-known fact that the availability of information of almost any kind to anybody with the requisite skills and equipment has increased enormously in recent years. Anonymity has all but disappeared. Information that is obtained from individuals, organizations and other entities is culled together and is accessible to interested parties at low cost.^{23[23]} The point of this is not so much the loss of privacy, but the fact that *nonrivalry* of products, which is one important factor in the evolution of the need for nonprofit organizations, is waning. Recall that the problem with nonrival products is that the selling organization cannot distinguish among consumers with different tastes (demands), and consumers, although wanting to receive better provision of the afflicted products, do not trust the motives of the for-profit firm and do not want to divulge to it their demand information, and do not want to allow it to charge them higher prices. The technology is moving rapidly in this direction in many areas, reducing the need for the special mechanism that nonprofit organizations provide.

A directly related issue concerns excludability. Once personal identity is established easily, the door is open to the introduction of charges and fees. With the rapid increase of financial transactions on the Internet, the time when very small charges can be made securely and at an insignificant transaction cost is almost here. Hence the *nonexcludability* attribute of products, which gives rise to the demand for the nonprofit form of organization, is waning too.

Other technological changes further reduce the nonrivalry and nonexcludability of products. Consider the distribution of information in the context of newspapers, radio, TV and the new media. The technological and economic possibility of satisfying specific

^{23[23]} When I dial the newspaper from my home to suspend delivery, the automated operator has no questions of me, only to confirm my house number, before proceeding to the dates of suspension. When I connect from my computer to the airline to purchase tickets, I do not need to identify myself: I just need to click on the 'purchase' button to execute the purchase that will be charged automatically to my credit card. The email announcements and the mail advertising I receive from different vendors contain customized information tailored to my tastes and preferences as expressed through past purchases in a variety of unrelated places that sell the information to interested parties. The supermarket that offers a free membership will track my purchases and will let me know when my favorite toothpaste is on sale, or will offer me a special bonus if it turns out that I seem to wander away to other stores. If I seem to make erratic purchases in strange places, the credit card company will call to make sure that my card has not been stolen. And much more is coming our way.

demands has grown enormously.^{24[24]} Whereas a for-profit newspaper, radio station and other local services were not long ago forced to satisfy the average demand of a local market, leaving room for consumer-controlled (and often consumer-run) nonprofit organizations to satisfy narrow niches, for-profit firms can now tailor their services to ever-narrower niches even in small markets, and certainly with ever-increasing markets that go beyond the local population. This development is made possible by the availability of technologies that allow inexpensive production of multiple variants of the same product, and the inexpensive exclusion of non-payers.^{25[25]} These trends are likely to reduce the demand for nonprofit organizations.

How about asymmetric information: is it also going away? The rapid collection and transmission of information improves consumer awareness and reduces asymmetric information in most areas of commerce. There are many dimensions to this issue; here I focus on one aspect only. In order to choose a product afflicted by considerable asymmetric information, consumers have a few options. First, they can just go to established organizations and hope that their sustained existence is proof of their reliability. Second, they may inquire about the reputation of organizations with which they consider transacting, seeking information through their social networks, consumer-oriented publications, professional organizations, and so on. And they have a third option, which is related to the previous two but fast outpaces them: information sources on the Internet. The Internet is abuzz with what appears to be the fastest growing niche, information brokerage. Information is available, and within a few years its quality and quantity will likely improve, about a large number of manufactured goods as well as services such as hospitals, physicians and day care centers. Reputations become enshrined in records rather than in social networks. This increasingly allows consumers to exercise control over organizations with which they transact in the standard market

^{24[24]} Just twenty years ago in the US, even the *New York Times* was available outside the New York City area only by mail, as were other domestic and foreign newspapers. Radio, especially foreign radio, was available during certain times of special broadcast, and on short waves only. Now newspapers print simultaneously in several locations using satellite technology, and are also available on the Internet. Radio broadcasting from an increasing number of stations from around the world, including small towns and university stations, is available on the Internet. And these services are already available on hand-held devices, whose quality will likely improve and prices decline.

^{25[25]} Whereas during the early years of e-commerce many of these services have been provided freely over the Internet (with funding by investors and advertisers), charging user or membership fees is rising fast, facilitated by the increased reliability of electronic financial transactions.

fashion: anonymously, in the ‘take it or leave it’ fashion instead of the ‘voice’ mode employed by consumers engaged in the control of nonprofit organizations. The information revolution causes the *asymmetric information* attribute of products, which has an important role in the existence of nonprofit organizations, to be reduced.^{26[26]}

The supply side – improved control over nonprofit organizations, and access to resources

The inexpensive availability of vast amounts of information may facilitate control over nonprofit organizations, and lower the cost of consumer participation in the affairs of nonprofit organizations as well as increase the effectiveness of their participation. Whereas, in the US, individuals would have had to exercise substantial effort to access financial and other information about nonprofit organizations of interest, such information is becoming increasingly available on the Internet.^{27[27]} This development will allow interested parties to perform comparative analyses of nonprofit organizations, giving stakeholders in nonprofit organizations power and eventually control over managers in a fashion and degree similar to those enjoyed by shareholders in publicly traded for-profit firms. Stakeholders and analysts will be soon able to examine ratios such as fundraising costs to total revenue and administrative costs to total costs, across organizations and over time, forcing discipline and control over administration of the sort they could never before exercise. As a result, the efficiency of nonprofit organizations and their ability to survive will be enhanced.

Additional salutary effects of the Internet and the communication possibilities associated with it similarly parallel developments in the for-profit sector. Just as the reach of for-profit marketers has been vastly extended with the aid of the Internet, so does the ability of nonprofit organizations to access broader swaths of potential stakeholders who might be interested in providing time and money to support certain products provided by nonprofit organizations. Particularly affected are nonprofit organizations that operate

^{26[26]} For a detailed examination of the role of information and reputation-building on the Internet, see Ben-Ner and Putterman (2001).

^{27[27]} Detailed financial information drawn from the federal tax files (Form 990) that US nonprofit organizations are required to file is available on line at www.guidestar.org and <http://nccs.urban.org>. Although not all categories of nonprofit organizations are required to report (see Ben-Ner and Van Hoomissen 1993, Figure 1, for information), this recent development will transform the informational landscape with respect to nonprofit organizations.

beyond local markets and whose existence depends on larger niche size than that which is available in a single geographic area.^{28[28]}

Likewise, access to capital is likely to improve for nonprofit organizations for several reasons. First, as information about borrowers is enhanced, lenders such as banks can be less discriminatory in their practices, relying on actual information rather than signals such as the type of organization when they make their lending decisions. Second, new financing and fund-raising tools are becoming available that will allow nonprofit organizations to raise more easily funds from donors. In the United States, some of the largest for-profit financial institutions are becoming quickly enormous fund-raising channels.^{29[29]} These developments will compensate in part for nonprofit organizations' competitive disadvantage in obtaining financing because of the absence of equity shares.

B. Market size

The size of the market on which both manufactured goods and services are transacted has been increasing. This trend is particularly significant for products that were produced and consumed in a restricted geographical area (including those that are termed 'local public goods' by economists). First, transportation costs have declined, and transportation has improved in both safety and speed. This resulted in the more efficient movement of goods to people and of people to services. For example, many thousands of people fly airplanes to watch a theatrical production or visit a museum exhibition; the effective size of demand for this sort of services has expanded in some cities substantially beyond the local market. This allows, for instance, mounting more niche productions oriented toward groups whose specific demand was met through local nonprofit theater or art institutes or was simply unmet.

^{28[28]} For example, www.VolunteerMatch.org enables volunteers to use the Internet to find volunteer opportunities by ZIP code, and onGiving.com allows nonprofit organizations to raise donations, as well as gives away advertising revenue to nonprofit organizations. There are numerous on-line organizations that fulfill similar functions and, just as with for-profit commerce on line, reputations and trust take time to establish; furthermore, the suffix ".org" does not provide a shield against the possibility of a for-profit operation under the guise of a nonprofit organization.

^{29[29]} Fidelity Investments, a large for-profit financial institution, has become the second largest recipient (actually, a channel like a community foundation) of charitable giving in the United States in 2000, after the Salvation Army (The Chronicle of Philanthropy, November 1, 2001). Fidelity's Charitable Gift Fund website at <http://www100.charitablegift.org/> also offers information that allows potential donors to understand better the organizational and financial affairs of the nonprofit organizations to which they consider making donations.

Second, transmission of data through various electronic media such as the Internet, CDs and DVDs make it possible to experience activities from locations other than where they are produced, generated or displayed. One can view a painting or a sculpture from multiple angles by moving the computer mouse around, and one can participate in a seminar discussion via a satellite link or the Internet at low costs. As a result, the nonrivalry associated with the kind of products exemplified above is declining, accompanied by clear opportunities for exclusion.

The consequences of these developments for the future role of the nonprofit sector are clearly adverse. However, since many of the existing organizations providing the kind of services described in the previous paragraphs are nonprofit, they benefit from the expansion of the market despite the fact that the rationale for their existence *as* nonprofit organizations is declining. Hence, in a curious fashion, although the rationale for the nonprofit sector as a sector distinct from the for-profit sector is weakening, it is likely that the organizations that comprise it will grow. Because administrators and others running these organizations have interests linked to the nonprofit status of the organizations and are generally unable to cash in from their transformation into for-profit firms, and as long as the legal framework remains in place, there will probably not be a phenomenon of decline of the nonprofit sector in these fields, any time soon.^{30[30]}

C. Mobility and migration, and community

The geographical mobility of people has increased as the mobility of goods and services rose. In many parts of the developed world, indicators such as the proportion of the population of a city that was not born in the city in which they reside and the average length of residence in a locality, suggest that the percentage of residents who have long-term connections to the localities in which they live has declined. This development has likely reduced the willingness of individuals to invest in the communities in which they live physically but do not belong emotionally or socially. This implies a weakening of nonprofit organizations, which require the willingness of individuals to make voluntary contributions of time, money and effort to nonprofit organizations. Such willingness

^{30[30]} See articles in Weisbrod (2000) showing that many nonprofit organizations grow to resemble for-profit firms.

depends on individuals' caring for the provision of goods and services to others (that is, seeing others' welfare as a public good), or being susceptible to peer pressure aimed at reducing free ridership and affecting positive voluntary action. Increased mobility reduces it all, harming nonprofit organizations' ability to act.^{31[31]}

A related factor concerns the support of for-profit companies for nonprofit organizations in the areas in which they operate and especially where they are headquartered. With the increase in the proportion of executives who operate away from their hometowns, the voice of executives in support of local contributions is muted. Hence charitable contributions by businesses will likely to be increasingly motivated by business reasons, and progressively less by interest in the communities in which they operate and in which their executives grew up.^{32[32]}

There is another effect of the trends in communications noted earlier, affecting the obstacles faced by nonprofit organizations and the associated costs of establishing and operating them. Nonprofit organizations require a degree of social cohesiveness in order to raise funds, to induce demand revelation, and to assert consumer control over these organizations. As the possibilities of forging community connections over long distances increase, the bonds that tie local communities weaken, to the effect of weakening nonprofit organizations. Alas, the communities forged on the distance-spanning Internet and other means do not seem to rely as much on common services as their localized counterparts, and if they do, they appear to work successfully with for-profit firms. Evidence for this is the rise of virtual communities sponsored, initiated, or facilitated by for-profit firms, such as those on Yahoo, AOL, and many other Internet portals.

A second-order weak effect may operate in the opposite direction. In stable communities trust in for-profit firms is created and maintained through the collective memory of the community who transmit the information from another and over time. When this mechanism is weakened by mobility, trust in for-profit firms selling products affected by asymmetric information will weaken, bolstering demand for nonprofit organizations.

^{31[31]} For an extensive discussion of this and other points related to factors that lower investments in social capital, see Putnam (2001).

^{32[32]} Nevarez (2000) investigates giving in California communities and finds that the giving patterns of new-economy businesses differ from old-economy companies; he also relates lower giving to the fact that business leaders in the new economy are new to the areas of their operation.

Mobility also tends to increase diversity as people from different backgrounds and cultures move and mingle. Diversity in the demand for products with significant nonrivalry and nonexcludability attributes such as in culture and education is a stimulus for demand for nonprofit organizations in these areas. Indeed, cities and towns around the world are experiencing a proliferation of small nonprofit organizations oriented to immigrant groups.

Finally, in a splintered society some people will desire to strengthen their belonging to communities. As noted earlier in the discussion of relational goods, such people may seek to attain this goal by forming or joining nonprofit associations. Moreover, some people will seek refuge from the commercialized and fractured culture by working in certain nonprofit organizations. These trends will have a favorable effect on the nonprofit sector.

D. Entrepreneurship

Individuals possessing skills, ideas, and excitement and who wanted to operate outside the mainstream of either the corporate world or government have in the past tended to work in social movements, voluntary organizations, and other nonprofit organizations (Mirvis and Hackett, 1983, Rose-Ackerman, 1996, Zimmermann, 1999). The new economy, with numerous entrepreneurial opportunities seems to be attracting similar people (Colombo and Delmastro, 2001) at the partial detriment of the nonprofit sector.^{33[33]} But as the new economy becomes institutionalized, some entrepreneurs may migrate to the nonprofit sector and strengthen it.^{34[34]}

E. Technological change and increased productivity

In the 1960s, William Baumol and William Bowen predicted the coming of technological improvements in production that will affect primarily the manufacturing

^{33[33]} Studies of entrepreneurs do not provide *direct* evidence on the statement in the text, nor are they comparable in the variables that they consider. It is my *interpretation* of the results that I state in the text, rather than the authors'.

^{34[34]} There is some anecdotal evidence that some individuals who became wealthy from new-economy ventures abandon them in favor of establishing new nonprofit ventures. This phenomenon is much discussed in the Seattle area of Washington State, where wealthy Microsoft (and other, less well-known companies) top employees and executives left their jobs to pursue philanthropic activities, often in the field of environmental protection and culture.

sector, which will consequently see productivity gains, while the services sector will lag behind. The productivity gains would change the relative prices between manufacturing and services to the advantage of the former. Furthermore, because the two sectors are linked through the labor market, in order for service industries to be able to attract workers they will have to raise prices, which will further change the relative prices between manufactured goods and services to the detriment of the latter. As a result, consumers will shift some of their consumption to manufacturing, causing a decline in services (Baumol and Bowen, 1966).

Recent developments have largely confirmed these predictions. Although the information revolution has aided many service industries at least as much as manufacturing industries, the impact has been uneven, and the Baumol-Bowen predictions were correct for many industries in which nonprofit organizations are prominent. Services that rely heavily on face-to-face interaction (or at least where the expectation is that this will be the case) have been put at a relative disadvantage. As Baumol and Bowen remarked, the strings section in an orchestra still requires a fixed number of violins – and violinists – in order to produce on stage a particular piece of music, and this number is unaffected by technological change. In order to educate students no fewer teachers are required today than in the past.^{35[35]} And to care for a person in need of personalized attention, at least as much time is required from a social agency staff person today as it was in the past. In these labor-intensive fields the productivity of operations (as distinguished from back-office administration) rose little in response to technological innovations, making other fields more rewarding to workers who otherwise would be musicians, educators, social workers, and to consumers who substitute less expensive services for the relatively more expensive ones. These developments strain the vitality of parts of the nonprofit sector, and strengthen only very narrow segments of it.

F. Changes in broad demand patterns

^{35[35]} The effect of on-line learning on the teacher/student ratio is unclear at this stage. At this time it appears, at least to this writer, that on-line higher education changes somewhat the nature of the educational product and perhaps the mix of different types of teachers, but not the said ratio. For an evaluation of the impact of technology on various industries, see articles in Litan and Rivlin (201b).

The distribution of economic activity across different types of organization is affected not only by the relative merits on the demand and supply sides of organizations, but also by the demand for products that is unrelated to the nature of the organizations that provide them. Changes in the demand for the products of different industries will likely change the distribution of types of organization; for example, an increase in the demand for products of industries where nonprofit organizations are predominant will increase the presence of nonprofit organizations in the economy (assuming that there were no offsetting changes). A detailed analysis of changes in demand patterns in the economy is well beyond the scope of this essay, but a few observations, even if extremely speculative, may be useful in order to suggest the direction for a more comprehensive investigation of the *net effect* of economic, technological, and other changes on the size and future of the nonprofit sector.

Two broad trends have had an important effect on the nonprofit sector in many countries, particularly the developed ones. First, since the 1980s, the composition of the GNP in many countries has been shifting away from manufacturing toward services. The nonprofit sector has benefited from the rise in demand for some of its services. Second, government involvement in the economy has been reduced in many countries. Although most of the reduction has been in manufacturing, power generation, communications, and other industries in which the nonprofit sector is not active, in some countries, including the US, there has been retrenchment of a variety of government services. Nonprofit organizations (as well as for-profit firms) expanded in these areas as governments transferred duties to them or when they entered to fill in a need that was no longer satisfied by the government. Overall, the share of the nonprofit sector in economic activity has risen in many countries during the 1980s and 1990s.^{36[36]} The forces that brought about these trends are still at work, although one would assume that the pace should slow down because of the limited remaining potential for change; continuation of these trends will exert pressure towards further increasing the share of the nonprofit sector relative to the for-profit and government sectors.

^{36[36]} For an analysis along these lines, see Ben-Ner and Van Hooymissen (1990), who examine changes in the sectoral distribution of economic activity in the US during the 1980s. For information about the change in the relative size of the nonprofit sector in various countries see the Johns Hopkins Comparative Nonprofit Sector Project (xxxx).

A reorientation of the values held by large segments of the population has been noted in many countries.^{37[37]} Of particular relevance here are the strengthening of self-interest and individualistic orientation at the expense of concern for others, and of the view that access to consumption of a wide variety of goods and services, from food and housing to education and safety, have to be earned through individual efforts rather than being anchored in basic rights for housing, minimum income and so on that are earned by virtue of membership in a community or society. This transformation has been already responsible in part for the reduced role of the government noted in the previous paragraph, but it may also erode support for nonprofit provision of related services. Nevertheless, as noted earlier, a community orientation remains in parts of society, and may even expand, fueling some demand for the nonprofit sector and supplying workers to it.

^{37[37]} See Ben-Ner and Putterman (1998).

IV. Conclusions

For a long period the nonprofit sector has enjoyed substantial growth, first in the United States where it has been growing steadily since the 1950s to encompass nearly one-tenth of total employment, to Western Europe where the impetus for growth has come in the 1980s, to the more recent growth in nonprofit activity in emerging market economies in various parts of the world. This growth came in response to various changes that affected the respective economies.^{38[38]} The changes that sweep the world now are likely to impact again the nonprofit sector. Will it grow again, or will it shrink? This essay identifies several, partly contradictory, trends that are likely to affect the future of the nonprofit sector. Although the essay suggests that, on the whole, the nonprofit sector may be disadvantaged in the new economy, a strong prediction is impossible to make.

The analysis offered in this essay suggests that there exists a demand for nonprofit organizations as solutions to problems for which for-profit firms cannot offer adequate answers. However, recent and continuing technological and economic changes tend to reduce the magnitude of these problems as well as enhance for-profit firms' ability to cope with them, consequently reducing the demand for nonprofit organizations. For-profit firms are most effective when they provide products that can be customized to consumers' individual needs (rival products) and for which a price can be extracted (excludable products), and when the products are sold to well-informed consumers (under conditions of symmetric information). Nonprofit organizations are most needed when products have substantial nonrival and nonexcludable elements, and are provided under asymmetric information. The technological revolution enhances rivalry, excludability and symmetry of information, and therefore nonprofit organizations are likely to be less needed. Globalization, the expansion of the effective market size, and other changes will likely enhance this trend.

There are also contrary trends that result in stronger demand for nonprofit organizations. For example, the anonymity of the Internet allows for quick entry and exit of companies, a fact that creates problems of trust that depress the reliance on Internet

^{38[38]} See Anheier and Ben-Ner (1997).

services. But information brokers, alliances between new Internet firms with established 'brick and mortar' firms, and increased government regulation and industry self-regulation, seem to improve the trust problem, leaving only limited room for nonprofit organizations to offer their own solutions.^{39[39]} Another example is provided by the increased mobility of people, which increases diversity of people and of demand for cultural, education and other services. These diverse demands are often best satisfied by nonprofit organizations. These contrary trends notwithstanding, the net effect of the various changes on the demand for nonprofit organizations will likely to be negative. [Diagram 3](#) encapsulates the predictions made in this essay for the demand for nonprofit organizations in some industries in which they are prominent in the United States.

The supply potential of nonprofit organizations, including the ability to run them effectively, is likely to improve thanks to various changes identified in this essay. Effective control and management require a lot of relevant information, which has been long lacking in the nonprofit sector. The information revolution is likely to improve drastically the situation, making the nonprofit organizations more efficient and more likely to be able to provide effective solutions than before.

The net effect of these two important and opposite effects, on the demand side and on the supply side, combined with other contradictory effects derived from other factors, make it impossible to predict the direction of change in the relative size of the nonprofit sector. My own sense is that the net effect will be unfavorable to the nonprofit sector, although not all organizations will be on the losing side. While there will be organizations that will see the demand for their products disappear, other organizations will enjoy improved controls and management and will enhance their viability to offset any weakening in demand.

Are there any policies that can counter these deleterious outcomes for the nonprofit sector? Some of the negative effects can be mitigated by steps taken to strengthen nonprofit organizations' ability to deal with problems associated with nonrivalry, nonexcludability and asymmetric information, and by improving operational efficiency. These steps can be accomplished by strengthening the role of consumers and donors in the organizations' governance to buttress claims for their being *bona fide*

^{39[39]} See Ben-Ner and Putterman (2001).

nonprofit and being truly operated for the benefit of consumers, and by improving consumer and donor control and oversight over management in order to operate efficiently.

Predicting the future is a risky business. There are at least a few places where the picture drawn in this essay may turn out to be wrong. First, the changes in technology may turn out to be less important than I anticipate them to be, and their effect on the specific demand for nonprofit organizations may likewise turn out to be negligible. Second, the big economic changes that increase the size of markets and the geographic mobility of people may be reversed because of political and security concerns. Finally, there may be political and social changes that draw communities more closely together.^{40[40]} Should these alternatives to the predictions made in this article come to pass, the nonprofit sector will not be diminished significantly, and may even benefit from them.

^{40[40]} It is difficult to predict the effects of the tragic events of September 11, 2001, and those that continue to follow them. In an interview with the Minnesota affiliate of the ABC TV network (aired on November 14 and 15, 2001) I commented that the three changes noted in the text may be among the consequences of 9/11.

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Diagram 1: Examples of Products with Different Attributes

Rival	Nonrival	Excludable	Non-excludable	Symmetric Information	Asymmetric Information
Soft drink	Ocean water	Soft drink	Ocean water		Soft drink ingredients
	National defense		National defense		
Theater seat, hall	Theatrical production	Theatrical performance	Theater hall		
	Car model	Automobile			Automobiles' reliability
	Quality of a product	Product			Quality of a product
	Color of a product				
Child care center	Child care quality	Child care center	Child care quality		Child care quality
Public health education			Public health education		
Patient treatment	Medical research	Patient treatment			Health care effectiveness
	Donations				Use of donations

Variable Factors Associated with Attributes

Marginal vs. fixed costs
affected by technology, market size

Exclusion costs
affected by technology

Information costs
affected by technology

**Diagram 2: Issues Arising in the Provision of Products by
Nonprofit Organizations and For-Profit Firms**

		<u>For-profit</u>	<u>Nonprofit</u>
<i>Demand side</i>	<i>Nonrivalry</i>	Heterogeneity of demand creates problems of measuring demand. Need information about specific groups' demand – consumers do not reveal it voluntarily because of lack of trust, and do not make donations.	Consumers and donors reveal demand and pay accordingly. Control ensures compliance by the organization with their objectives..
	<i>Nonexcludability</i>	Cannot charge economic price.	Same as above.
	<i>Asymmetric Information</i>	Firms may take advantage of informational advantage ⇒ consumers do not trust firms; trust, reputation, regulation, and warranties remedy the problem.	Absence of profit motive and consumer control generate trust.
<i>Supply side</i>	<i>Entrepreneurship</i>	Private provision for private gain ensures supply.	Absence of profit motive limits provision of initiative.
	<i>Capital</i>	Supplied in the expectation of future profits.	Absence of profit motive denies access to equity capital.
	<i>Control and Management</i>	Exercised by owners and their agents, through the threat of takeovers, and through the threat of withdrawal of capital by shareholders.	Control by customers is limited because of costly individual effort but diffused benefits. Concentrated ownership, takeover threat, or markets for shares that improve control cannot exist.

Diagram 3: Partial Summary of Predicted Changes in Product Attributes and in the Demand for Nonprofit Sector Services, Selected Industries

<i>Product Attributes</i>				<i>Demand</i>		
Industry	Non-rivalry	Non-excludability	Asymmetric Information	Specific for nonprofits	Specific for Product	Total for non-profits
Health Services	↓	↓	↓	↓	↑	?
Education and Research	↓	↓	—	↓	↑	↓?
<i>Libraries</i>	↓	↓	—	↓	↓	↓
Social Services						
• for the poor	↓	—	↓	↓	↑	?
• prisons	—	—	↓	↓	?	?
• for ethnic groups	↑	—	↓	?	↑	↑?
• child/old people care	↓	↓	↓	↓	?	↓?
• Clubs and associations	↑	↑	—	↑	↑	↑
<i>Arts, Culture</i>						
• Museums	↓	↓	—	↓	↑	?
• Theater	↓	↓	↓	↓	↑	↓?
• Radio, TV	↓	↓	↓			
Religious Services	↓	↓	↓	↓	?	↓?

Notes: ↑ indicates increase, ↓ indicates decrease, — indicates no change, ? indicates indeterminate prediction

