HOW TO BUDGET DURING COVID

What to do with your 2020 operating budget

What are the most important areas to budget for?

How to budget today for what might happen later?

Taking advantage of the down market

"The only way for your budget to remain relevant right now is to focus on short term, responsive, priority-driven budgeting processes."

THROW AWAY YOUR 2020 BUDGET

In this current market, we don't know what will happen more than a few weeks from now, let alone how the end of the year will pan out. For most of you (probably all of you), the budget you created last year is already irrelevant. That being said, we are encouraging most of our clients to move to monthly budgeting.

The purpose of monthly budgeting is to force leadership into conversations about the highest and best use of funds in an environment where flexibility and adaptability mean the most. The priorities you had in January are not the same now and you are continuing to learn more and more about which adaptations are working and which are not. The only way for your budget to remain relevant right now is to focus on short term, responsive, priority-driven budgeting processes.

BUDGET FOR...NOTHING

"Cash is king" is a true and popular statement, but in a time of crisis, it becomes even more important. In the budgeting process, there may not be a more important line item than savings. We have talked extensively in our previous content about ways to save money on mortgages, rents, and other items. While there is popular conversation over whether or not this pandemic will ultimately impact top line revenue negatively (giving), the bigger conversation needs to be around how it can impact our bottom line positively (profitability). You read that correctly: it's ok to be profitable as a non-profit. After all, not-for-profit is a tax filing status, but it was never intended to be a business model. By not having weekly service, there should be an enormous amount of savings going directly to the bottom line. You do not have to find ways to spend that money!

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BUDGET FOR SURVIVAL

Right now, due to the PPP loans and a population which has remained confident in the economy despite the COVID pandemic, our church clients have, for the large part, been completely insulated from any major financial impact. However, that’s not promised forever. There are conversations about this pandemic lasting through the year, even making a resurgence in the fall. More importantly, we have to ask ourselves what the post-pandemic impact will be. Will people come back to assembly just because they’re allowed to? Doubtful. After all, the governor of Georgia announced last week that he was opening many non-essential businesses (restaurants, tattoo parlors, bowling alleys, etc.). Want to know what happened? Atlanta was a ghost town. Just because people could go out did not mean they did. They chose not to. Restaurants did not open. People stayed home. I did consider getting a tattoo. (just make sure it’s spelled correctly)

COVID has completely reshaped the business to business and business to consumer relationships. Consumers are building completely new habits that will last once the pandemic is over, and we simply don’t know what that means. So, our advice is to be ready for a deferred economic hit. Consider that when you are able to host services again for the first time, people will still stay home. What we are learning about serving people in this virtual environment is going to inform our post-pandemic cultures. There will likely be a rainy season coming, and the organizations who have created a strong cash position will have the opportunity to survive change without the pressure of an undue financial burden.

> “There is no better time to take advantage of opportunities than when a market is down.”

BUDGET FOR OPPORTUNITY

There are far more great opportunities in bad markets. In the real estate world I came from, developers loved down markets (if they had sold off their assets, of course). Why? There is no better time to take advantage of opportunities than when a market is down. Basic economics teaches us that when there are more sellers than buyers, prices decrease, and opportunities to pick up distressed assets increase. Remember a few years ago when all of our churches could go buy a single tenant retail building (aka “big box store”) and convert it into a church at a low cost? That’s coming back, and soon. Construction costs will be down, and retail is going to go through an extremely tough recovery period. Where we haven’t had solid options for big box conversions in the past few years, we believe that there will be a swath of those types of properties hitting the market in either sale or lease opportunities. Church acquisitions/mergers have already been trending heavily up in the past few years, and this crisis will add a major accelerant to that already popular and growing trend.

IN SUMMARY

The churches and organizations which have stockpiled their cash are in a place to jump on those opportunities and maximize potential value. It is very important that while we are in a period of insulation from a longer-term economic impact, building your war chest as large as possible while times are still good is the most important thing you can do from a stewardship perspective. In a situation like our current one, your war chest is no longer your reserve; it’s your future survival or opportunity fund.

STATUS OF THE MARKET

How are the current markets affecting churches?

What is happening in banking?

What to do with your debt

Falling construction prices

Church mergers and acquisitions

"While all of the key signs of economic downturn are present ...this is still different."

This is not the 2008 financial crisis. While all of the key signs of economic downturn are present: falling commodity prices, a sudden and unexpected crisis, economic over-leverage, and an unstable currency market...this is still different. The 2008 financial crisis was caused by Wall Street creating mounds and mounds of leverage upon leverage (remember credit default swaps, anyone?), along with an unprecedented artificial demand in housing, which in turn created over-inflated prices. The biggest difference is 2008 was truly the economy collapsing as our banking and capital markets system completely failed us. The recovery was slow.

The 2020 COVID-19 crisis is simply not the same thing. The recovery time from this should be much, much faster than 2008 and here is why. Is there still an unprecedented amount of debt in the market? Yes, but very little of it is low-rated junk bonds and "side bet debt" like before. It's mostly corporate and investment real estate debt, and it was taken out intelligently considering the low cost of money in the past several years. The demand in the economy is still very present, we just don't have access to supply as we sit at home and learn a new way of life. No one knows when this will turn, and obviously the sooner the better, but if we can stay afloat long enough to last through this "shelter in place" and keep the banking system from collapsing, we will recover quickly.

Organizations are learning how to adapt. And as in every crisis, there are organizations which not only survive, but thrive, and emerge stronger than ever before. We do not have a crystal ball, and no one should really be predicting anything outside of the next few weeks, but we wanted to point out several areas where churches have an opportunity to take advantage of current market conditions and put themselves in the best possible situation to take advantage of opportunities. Below are a few examples of things that are happening in the market as of right now, and we will dive into them in the rest of this email.

- Credit Markets have frozen (banks are not lending money)

- The stock market had a fear-driven sell-off as a result of the COVID-19 announcement

- The markets continue to fluctuate based solely on the news of the day

- Class A Office and Multifamily development is forever changed

- Construction prices should drop going into 2021

“But there is more going on than meets the eye.”

THE CHEAPEST MONEY YOU CAN’T GET....YET

The first thing to know is that banks are not lending money--at least not right now. This is especially true for churches, whose business model is based on assembly, which is currently banned. Banks are shuffling their commercial real estate lenders into pursuing loan modifications for their customers in an effort to avoid a mass delinquency rate across the board. Tenants are negotiating with landlords to not pay rent, and landlords are negotiating with banks to keep them afloat long enough to survive. Banks are also shuffling people to handle all of the Payment Protection Program (PPP) loans that are in masse.

But there is more going on than meets the eye. Mortgage interest rates are greatly affected by the bond market, which is in complete turmoil as investors are selling off bonds to raise cash (liquidity). When something like this happens, it drives interest rates down, and quickly, from an already very low point. As an example, early last month our company was working on funding for two large multisite churches, and we received multiple term sheets from various lenders with long term, 10-year fixed debt between 3.1% and 3.25%. Just a year to a year and a half ago, that rate was in the mid-5’s.

> “In short, banks should/could be lending money again within the next month, and interest rates will be very, very low.”

So here are some practical steps to take advantage of this. Based on every economic study we can see, the credit markets are going to open back up before the stock market and the bond markets recover completely, hopefully in the next four weeks. In short, banks should/could be lending money again within the next month, and interest rates will be very, very low. For anyone with any level of significant debt, you have the opportunity to refinance your existing debt into a long-term, fixed rate loan in the low 3’s. What we don’t know is how long it will take for the bond markets to recover, which would drive those prices back to either the high 3’s or low 4’s for low risk borrowers. While that is still a great opportunity, we feel that those churches who have a financial package ready to go will be in a better position to move quickly while the rates are still low.

To better understand how to work with your current bank or landlord through this crisis, please see our blog post: ***Managing Finances to Thrive in Crisis***.

EVEN WHEN CREDIT MARKETS OPEN, IT WILL BE TOUGHER TO BORROW MONEY

Things have seemed to roll along easy street since the recovery of the 2008 financial crisis. However, under our noses, our large corporations and real estate investors have borrowed a lot of money. I mean, a lot. Interest rates have been so historically low that it just made too much sense to borrow money and focus on using cash and surplus to invest internally and through acquisitions, where the return on investment is far higher than the cost of money.

There are a few things that cause a global markets crisis: commodity prices (bonds) falling, the economy being hit with something sudden and unexpected (COVID-19), and over-leverage (debt). All three of these are present at the moment, along with a stalling Class A Office market and slowing multifamily development. Churches are redefining themselves, and no one really knows how to underwrite that. What does that mean? Banks are a little scared. People have a lot of debt, and there are already questions outside of COVID-19 on whether the credit markets were due a season of tightening up, anyway.

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However, banks will still be in the business of loaning money and taking deposits. Churches that are going to be successful in borrowing money are going to have to have a higher level of quality in the packages that are being presented, and a much higher level of quality in their financial statements. Just always remember that when a credit officer is forced to assume something, he or she will always assume the worst. We have to do a great job of making the decisions easy for nervous lenders.

Construction prices are dropping, hopefully
Before COVID-19, there was already a lot of chatter about the construction industry, which has been hotter than ever in history. After the slow recovery of the 2008 fallout, there was an enormous pent up demand in the years to follow, which was met with a lack of workers to meet the demands. This drove up labor and materials costs to obscene levels.

However, that may be changing. There is an enormous amount of Class A office renewals hitting the market at the exact same time as a large load of new inventory. According to Costar, the largest aggregator of real estate data, the multifamily market (apartments) is in jeopardy of being overbuilt. Some markets, like Houston, have even red-lined (disallowed) multifamily development. Now, with COVID-19, many struggling hospitality companies (restaurants and hotels) may not survive. So what does all that mean? Less construction. Two years ago, general contractors and subcontractors had a backlog for two to three years. Now, at least in some markets, contractors don't have enough current work to finish the year.

For those of you who are in the planning stages of a construction project, this poses an enormous opportunity. Most people are still using "current" prices, but know those prices are still being based on having more work than they can deal with. The market has not yet adjusted. Expect for contractors and subcontractors to get much, much hungrier and aggressive over the next six to twelve months. Do we have any idea how significant the price drop will be? No. What we do know is that it will be a lot more competitive than it has been on both materials (suppliers) and labor (subcontractors).

"...just over 25% of the churches in America are somewhere between dying and life support."

CHURCH MERGERS

According to Jim Tomberlin and Warren Bird, who wrote the book Better Together: Making Church Mergers Work, just over 25% of the churches in America are somewhere between dying and life support. Based on our research, a lot of this has to do with gentrification and cities reforming themselves, where urban areas are being reformed and the small congregations of urban churches are selling their homes for high prices and moving to the suburbs. However, as we stated in the first paragraph, the churches who are successful right now are so because they were prepared. The churches that didn't have a digital platform and online giving are being hit, hard. Our prediction is that through this crisis, these churches who were already dying, or on life support, will not survive this.

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Also based on the research of Jim Tomberlin and Warren Bird, nearly 60% of all multisite growth in America in 2019 was through church mergers. If it is the case that churches who were already struggling will need a life raft, then there should be ample opportunities for healthy, growing churches to have more opportunities than ever to acquire relevant and useful real estate.

If you have any comments or questions on how your church can take advantage of any of these opportunities, please contact us at ***contact@ministry-solutions.com***.