Economic Forecast and Impact of Inflation on Revenue and Compensation

Nonprofit leaders need to make strategic decisions amid ongoing uncertainty. We examined the current economic forecast and the impact of inflation on investments, contributions, and employee compensation during the CapinCrouse National Nonprofit Virtual Seminar on February 8, 2023.

Stan Reiff, Partner and Professional Practice Leader – Consulting at CapinCrouse, moderated the discussion with these panelists:

- Jerry Bowyer, Economist, Author, and Columnist
- Bryan Taylor, CEO and Chief Investment Officer, Cornerstone Management
- Kelsey Helmick, Executive Compensation Program Consultant, CapinCrouse

This article highlights key takeaways from that conversation.

Stan Reiff: What is really going on in the economy, Jerry? Is a recession imminent? Are we already in a recession? What is your professional take as an economist?

Jerry Bowyer: I am an economic forecaster, so people ask me to predict the future of the economy every day. But while economic forecasters might be able to know a bit about what to expect in the near future, God is the only one who is omniscient. That being said, I do have some insights about the markets that I study as well as some observations from the past few years.

When we think about "markets," we are really talking about groups of people who interact with money, either by buying, selling, or saving. In addition to the very public markets such as the stock market, I also study several hundred other lesser-known markets that provide context for the current behaviors of the economy, as well as a glimpse into what may be expected.

Looking back at 2022, the U.S. technically met the definition of a recession during the first two quarters of the year. And it appears that we might be headed into another mild recession in 2023. There were many variables contributing to those two consecutive quarters of negative growth in 2022, including the ripple effect of COVID containment efforts in 2020. When malls and stores were required to close (resulting in some closing permanently), the unintended consequence was the reduced consumption of goods and services, which created more money in the market and ultimately led to the inflation that we have been seeing in the past year. The markets knew that inflation was coming back in 2020, but the Fed was in denial until they saw its impact.

An additional consideration is short- and long-term worker shortages caused by America's rapidly aging society and slow population growth. An economy grows only when there are more people and the people are more productive.

Stan: How should nonprofit leaders be thinking about the economic considerations you outlined in terms of their budgets and finances, both now and moving forward?

Jerry: Something that I talk with nonprofit leaders about is the multi-dimensional tension that inflation causes and how this can actually be beneficial for giving. In times of social disruption, inflation, and stagnation, charitable giving experiences a strong return, as it is in today's climate. Additionally, the inflation and interest rates we have been experiencing have strengthened the dollar, which means that American nonprofits working in emerging and frontier markets are benefiting from premium value creation in those markets.

Stan: Bryan, what impact are you seeing on nonprofits when it comes to donor attitudes and actions in the investing space?

Bryan Taylor: As you mentioned, the main impact on nonprofits has been in the areas of donations and investments. With the money in equity markets decreasing last year, yields in bond markets climbing significantly, and the high value of the dollar, we at

Cornerstone Management believe that interest rates and inflation may recede some, but will remain relatively high compared to previous years. The long-term trend in the market has been that investors will earn on cash. And while in the past 15 years we have adjusted to the reality that these earnings will be limited, in today's economy, it is imperative for investors to move their cash to avoid a negative fiduciary response.

I would love for Jerry to dive a bit deeper on the dollar right now, as I know that as the Fed peaks, other central banks will catch up. I wonder if there are other insights on this that Jerry could share.

Jerry: The dollar has already peaked, so it is in the process of moderating. During the era of the Trump tax cuts, when it was advantageous for U.S. companies to spend and invest in foreign markets, we all knew that the boomerang would eventually turn back around and those profits would make their way back to the U.S. This has been occurring recently, but it is unclear how long that window will remain open.

Bryan: Thanks for that, Jerry. I think it is important for nonprofit leaders who are working in other countries to keep that in perspective. I also think that nonprofit leaders should have a good handle on their treasury management policies to maximize their effectiveness.

When it comes to the economy's effects on the nonprofit donor base, one of the factors, as Jerry pointed out, is the challenge of people supply. When there is too much money in the market and not enough workers, the result is inflation. One benefit of not having enough workers, however, is low unemployment. And as mid-level donors remain employed, their giving remains solid, regardless of the state of the economy. Inflation and the market's volatility do have a negative impact on major donors, though. Major donors are affected by the higher cost of employment, higher liquidity, and tighter monetary policies that correlate to uncertainties in real estate and other major assets.

Stan: What are you seeing at Cornerstone in terms of investments?

Bryan: While there are some long-term challenges related to operating reserves and endowments, there are plenty of opportunities in fixed income. As interest increases, this also changes the multiple that people are willing to pay for future earnings. There is less risk in using cash for short-term gains rather than long-term. Along with that, there are opportunities in the gift annuities space for those major donors who are fearful of the stability of their major assets.

Stan: Transitioning over to the compensation piece of the discussion, Kelsey, what have you seen in the latest research? And what have our nonprofit clients been telling you about their compensation decisions amidst the current inflation?

Kelsey Helmick: The Bureau of Labor Statistics just released their December 2022 data, which reveals that the cost of employment to employers increased by 1% in the fourth quarter of last year and increased a total of 5.1% from December 2021 to December 2022. That has a real impact on compensation decisions when costs for employers have already risen before pay increases are even discussed. Since wage pressure increases in lockstep with inflation, there is additional pressure on the employer to make pay adjustments to remain competitive, but that isn't always possible with the nonprofit budget.

We have seen many of our clients opt for spot bonuses and other one-time benefits, such as flex time or gift cards given to their employees, rather than significant pay increases that will set a precedent for future years. Additionally, since the current economic climate has a disproportionate impact on the lower-wage earners in organizations, some of our clients have offered tiered incentives or pay adjustments that are higher for individual contributors than for management or leadership.

We recommend that our clients put together a compensation philosophy and policy document that can provide guidelines for what the organization believes about compensation and how those beliefs trickle down to compensation decisions. It is important for organizations to have this philosophy and policy documented before uncertainty arises, so all stakeholders are on the same page about how these situations will be handled.

Stan: I have a final question for Jerry and Bryan. Ministries can face a moral incongruence when their money is invested in companies that don't share their beliefs. Essentially, ministries could find themselves

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funding things they are against. Do you have any recommendations or resources for nonprofit leaders in this situation?

Jerry: I think it comes down to investors' responsibility to be aware of what the organizations they invest in stand for and to recognize that as shareholders, investors have a voice. Many people forget that the shareholders are the ones who hire the board of directors. Use your proxy votes, attend the annual meetings, ask questions, and raise concerns. When we show up, things change.

Bryan: I will also mention that one of the freedoms granted to us as Americans is economic advocacy, but we as Christians often miss the opportunities before us. By not speaking, we are giving up our rights.

Stan: Thank you all for your insights and contributions.

Please contact us with any questions.

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