Impact of inflation on community organisations and communities

Introduction

SociaLink has undertaken some research about the impact of increasing inflation on community organisations and communities to help inform SociaLink's understanding of pressure points and to provide insight to funders. SociaLink collated relevant research and surveyed local not-for-profits to gain insight on the impact of inflation locally.

The following report includes information about:

- Definition and causes of inflation
- Effects of inflation
- Measure of inflation
- Why inflation is high now?
- Implications of the pandemic and inflation for the community and not for profit sector including organisational costs, income and demand for services
- Ideas on what the sector can do to address inflation
- A summary of the responses from local organisations about the impact of inflation

Recommendations for funders are:

- If funders are providing multiyear grants, review agreements to ensure CPI accurately reflects increases in inflation.
- Ask applicants to ensure funding applications reflect inflation, particularly in staff and transport costs.
- Ask applicants if they are projecting an increase in demand for their services due to inflation increases.

Definition and causes of inflation

Inflation describes a rise of average prices through the economy, and means that money is losing its value. The underlying cause is usually that too much money is available to purchase too few goods and services, or that demand in the economy is outpacing supply. In general, this situation occurs when an economy is so buoyant that there are widespread shortages of labour and materials. People can charge higher prices for the same goods or services. Inflation can also be caused by a rise in prices of imported commodities but is usually transient and less crucial than structural inflation caused by an over-supply of money[1].

Effects of inflation

Inflation can be very damaging for a number of reasons. First, people may be left worse off if prices rise faster than their incomes. Second, inflation can reduce the value of an investment if the returns prove insufficient to compensate them for inflation. Third, since bouts of inflation often go hand in hand with an overheated economy, they can accentuate boom-bust cycles in the economy. Sustained inflation also has longer-term effects. If money is losing its value, businesses and investors are less likely to make long-term contracts. This discourages long-term investment in the nation's productive capacity.

Measure of inflation

The consumer price index published by Statistics NZ is the way New Zealand measures inflation. It records the change in the price of a weighted 'basket' of goods and services purchased by an 'average' New Zealand household which are grouped into categories (eg housing and utilities). The contents of the basket are defined by Statistics New Zealand, which periodically reviews and re-weights them, using data obtained from their annual Household Economic Survey. This is necessary because the basket of goods and services purchased by the average household will change over time.

Why is inflation high now?

Annual inflation has hit a three decade high at 5.9% from the December 2020 quarter to the December 2021 quarter, the biggest movement since a 7.6 percent annual increase in the year to the June 1990 quarter, according to Stats NZ (NZ Stats 27 January 2022)

The main driver for annual inflation is the housing and household utilities group, with prices for construction and rentals for housing increasing. Construction firms have experienced supply-chain issues, higher labour costs and higher demand which has pushed up the cost of building new houses. The next largest contribution to annual inflation is from the transport group with increased prices for petrol and second hand cars. Petrol prices increased 30% in the year to December 2021 quarter. There were also increases in the prices of computers and mobile phones as well as clothing and footwear.

Other countries in the OECD are experiencing higher inflation than in recent decades and are implementing measures such as raising mortgage interest rates.

Unemployment has fallen to a record low (3.2% for the three months ended December 2021), while wage inflation has risen to its highest level in a decade [2]. According to Stats NZ, the underutilisation rate, which is a measure of the slack in the labour market, was unchanged at 9.2 percent, the lowest since mid-2007. Unemployment is defined as those actively seeking work, while underutilisation includes those wanting to work more hours or who could work but are not actively seeking a job. The data was roughly in line with expectations for a steady unemployment rate, modest job growth, but a solid lift in wages.

[1] **Reserve Bank of New Zealand Fact Sheet: What is Inflation**

[2] Unemployment hits record low as wage inflation peaks, Radio New Zealand 2 February 2022

Recruitment agencies have said the employment market continued to favour job seekers, with feedback from customers indicating counter offers on wages and a likely upward push on them. The Covid pandemic had made differences to recruiting, especially continued widespread candidate shortages, changing career priorities and remote work advancements.

What does this mean for the community, not for profit, social sector?

The Covid 19 pandemic has already had a significant impact on the operations of community and social sector groups, as well as the communities they are serving.

The rise in inflation will compound these issues.

Pandemic Impacts that have been noted

- Lockdowns and alert levels have resulted in shut downs of all or part of their activities. For example hospices have had no trading revenue from their shops during these times, which are a significant source of income.
- Most charities do not have significant resources to fall on and are reliant on ongoing revenue streams, which was predicted to be increasingly difficult due to the pandemic and its effects on government efforts to minimise the impact, on the economy and on consumer behaviour. According to Martin (2019)[3] a provider in a financially sustainable position should be able to allocate at least 5% of their total expenditure to reserves, or at least three months' operating costs but a sample of annual reports indicated the average margin was 2% of total expenditure.

Affected revenue sources include:

- Donations, grants and other fundraising
- Fees and subscriptions
- Trading revenue from sale of goods and services
- Interest and dividends

These are impacted given:

- Gaming trust proceeds have diminished as pubs and bars have been closed or operating under restrictions.
- Philanthropic organisations have had reductions in their revenues and have less to pass on to charities.
- The public may tighten their belts and donations are likely to reduce.
- Many fundraising events cannot happen.
- Trading operations such as op shops and cultural and artistic events have been closed down or operating under restrictions.
- Returns on investment have taken a hit, albeit that this may be temporary. Interest revenues are at all-time lows and other equity-type investments have been rocked with volatile share market fluctuations.

[3] Jenkins, M (2019) Social Service System: The Fundign Gap and How to Bridge it. Social Service Providers Aotearoa

How will a rise in inflation affect the community/not for profit sector?

The JB Were's 2021 New Zealand cause report [4] identified the overall picture of the not for profit sector:

- Sector income growth rate over the last decade averaged 7% pa – against an expense growth rate of the same or slightly higher keeping operating surplus at or below 10%. Organisations are consequently operating on tight margins, which leaves little room to improve overall resilience and explore innovation.
- The sector's labour force saw changes in the increase of full-time staff and the shift from permanent part-time to contract staff as we continually move in the direction of a gig economy.
- The report's financial period researched was 31 March 2020 (a week before Covid-19 locked the country down for the first time). Analysis drew upon 400 charities with later return dates to provide a picture of the first six-months impact of Covid on the for-purpose sector.
- Evidence of Covid accelerating existing trends is evident. The hardest hit (50% loss of revenue) were those event-heavy sectors like Sport and recreation and Arts, culture and heritage, as well as the Social services working intimately with the most vulnerable in our communities. The Government wage subsidies helped some, but not uniformly. As a whole, the sector is 'doing even more for less', with already thin operating margins and only modest reserves to draw on to meet any covid triggered operating deficits.

Inflation is considered likely to impact in three ways according to an article based on the UK situation[5]:

- Rising costs – particularly for staff
- Depreciating income
- Impact on beneficiaries' finances changing demand levels.

1. **Rising Organisational Costs**

Research in the UK has found staffing costs account for 37% of total charity sector expenditure. To ensure that wages did not fall in real terms as a result of inflation in the UK (5.4% in December and predicted to peak at around 6% in April), charities would need to increase total wages by 8.8% from 2021. The sector was noted to already have issues with low pay, with the Living Wage Foundation finding that 17% of all third sector workers earning less than the real Living Wage, which jumped to 29% of all part-time sector workers, the majority of whom are women.

Anecdotally, staffing costs in the social sector in Aotearoa is considerably higher that the proportion of staffing costs outlined above for charities in the UK.

If salaries started to reduce in real terms, it was thought there was a risk of significant staff churn in the sector, and could mean charities might struggle to replace staff. Many were already experiencing a shortage of job candidates. This is within the context of labour shortages facing most industries

[4] Morrow, J and Mcleod, J 2021 New Zealand cause report, JB Were 2021 https://www.jbwere.co.nz/latest-insights/philanthropy/jbwere-nz-cause-report-2021/

[5] O'Halloran, J Rising inflation: What do charities need to know, Pro Bono Economics, 19 January 2022 https://www.probonoeconomics.com/news/rising-inflation-what-do-charities-need-to-know

nationally and locally. Salaries failing to keep up with inflation will likely exacerbate the skill shortages.

O'Halloran noted "it is important for charities to be thinking about wage negotiations as early as possible, while also realising that many of their staff are likely to be struggling already."

Other impacts of Dealing with the fall out from Covid include exhaustion and burnout in some sectors, in the US for example (may be relevant here) including child welfare, mental health and other direct services where demand has soared straining already stretched staff. Education and human services disproportionately employ women who have borne the brunt of child care issues. While the pandemic will eventually ease, there may be long term consequences if people leave the field in search of better pay. They are unlikely to return and a good wage will be needed to attract students and younger people.

Do Good Jobs online jobs board has recently published tips for the for purpose sector in thinking about the staffing situation and retaining staff:

https://dogoodjobs.co.nz/5-steps-to-retain-staff-during-the-great-resignation/

2. Depreciating income

The cost of living squeeze resulting from inflation may affect the level of donations to charities. O'Halloran considers there are three prominent areas of charity income that are vulnerable to being substantially affected by inflation.

- 1. Anchored donations, meaning those anchored in time through a historic direct debit, or those anchored in certain norms, where individuals have a set amount in mind that they wish to donate. The set amount eg $20 is unlikely to change with inflation but its value will depreciate. Therefore it's important for charities to discuss around levels of giving by donors, especially those on direct debits and update estimates of what services cost to deliver as inflation continues to drive those figures up.
- 2. Grants that have been recently awarded will significantly devalue in 2022/23. If an organisation was awarded a grant of $100,000 per year in 2021 for the next three years, the 2023 grant would be worth $94,000 after accounting for inflation, a reduction of 6%.
- 3. The sector as a whole is a net saver, not a borrower. With high rates of inflation, money held in reserve is at risk of losing its value which should prompt further discussions about investment strategies for those organisations with reserves.

3. Changes in demand due to the cost-of-living squeeze

The most deprived households' budgets, already under severe stress, will be most affected by inflation and drive high demand for services provided by charities.

For the average renting family the cost of living went up by around $50 a week over the last year, while income went up by about $25 a week.

With stretched income going to towards rent or mortgage repayments there is little flexibility to cut costs. It has been observed that price increases for food, transport and housing are particularly harmful for low-income households, resulting in an increase in need for foodbanks.

Benefits are scheduled to rise by $15 after tax from 1 April 2022. This is likely to be absorbed by increased prices so in effect it isn't a 'real' increase and indeed may mean a fall in the real value of benefits. This will drive more people into deeper poverty and is likely to drive up demand for services.

This will also affect community groups in the arts and performance sector as inflation means less disposable income to purchase tickets or spend on entertainment and leisure experiences.

Reports of the impact of inflation

- People needing more help: eg twice the number of meals when receiving Meals on Wheels per week, needing more assistance from foodbanks which are seeing increases in price of food while serving double the number of clients a year ago.
- Suppliers charging more for food that social services serve eg nutritional drinks like Ensure gone up 10%. Coupled with increased fuel prices, driver and worker shortages mean it is costing more to provide the same services
- On top of the usual need, white-collar workers and double-parent families are increasingly struggling to pay mortgages and are asking for help to put food on the table.
- In early 2021 Tauranga the Tauranga Community Foodbank saw a 33% increase in demand in 24 months, the cost of housing being a major contributor as well as seasonal blips such as costs involved in returning to school. A massive increase in solo people reaching out, including older people living on superannuation, and single people on minimum wages.[6]
- In September 2021 Foodbank Canterbury distributed 103 tonnes of food – about 294,000 meals to more than 150 agencies in the Canterbury area. In 2020 it distributed about 30-35 tonnes a month.

What can the sector do?

It is important for boards and leadership teams to factor higher than anticipated costs into any planning assumptions.

The key messages from this analysis for charities is that they need to:

1. Determine if the demand for their services is likely to change and plan for it.
2. Enter wage negotiations early and appreciate many are likely to be struggling.
3. Revise income targets and plan how to deliver them in the context of inflation.

Suggestions put forward by a collective of charity, non-profit and community groups to government suggested ways the Government could assist to alleviate some of the financial pressure:

- Emergency stabilisation fund
- Special low interest loans
- Tax relief to incentivise donations

[6] https://www.rnz.co.nz/news/national/436948/demand-for-food-parcels-and-housing-soars-in-bay-of-plenty

- Dedicated support to provide assistance to unique challenges faced by the sector.

The Government has tried to offset the financial burden felt by many to due to Covid-19 with a number of financial packages. This included $27 million for essential services in the social sector to ensure such services can continue to assist during the lockdown.

Other options suggested by the Institute of Directors were:

- Applying for the wage subsidy scheme
- Considering options to use your organisation's emergency funds set aside for a 'rainy day.'
- Virtual fundraising – creating an online fundraising plan
- Getting advice from an independent advisor.

Thinking longer term, while acknowledging the difficulty of doing that when charities and other groups were just trying to get by day to day, it could be the chance to look for a reinvention.

- Strategic thinking is more essential than ever – what has been outmoded or part of tradition in an organisation that needs to be trimmed back or thought through.
- Consolidation with other charities with the same aim and purpose?
- Consider new opportunities and resources

Local Survey of Inflation on Community Organisations and Communities

Twelve organisations/respondents did the survey. Of those:

- 3 were small (0-3 FTE or under $100,000 revenue
- 5 were medium size (4-8 FTE or revenue between $100-$700,000)
- 3 were large (9+ FTE or revenue over $700,000)
- One respondent did not answer this question.

Summary of results

- For organisations, staff salaries/wages and travel/vehicle costs are the two main areas where rising costs are expected to have high impact. For some organisations, salary costs are a key expense and they expect demand for movement in this area from employees but may struggle to increase wages and even cut hours because of reduced revenue. It was noted revenue from various sources would need to increase by the rate of inflation just to break even.
- Rising costs are considered to have a high impact on financial stress in communities and to a lesser extent on food and housing demand.
- Mental health stress and anxiety are observed as a key impact for individuals and families as they deal with ongoing Covid issues, rising costs and reduced health care access (due to Covid).
- The results of the survey largely mirror the accompanying commentary regarding the impact of inflation on community organisations and communities.

Recommendations:

- If funders are providing multiyear grants, review agreements to ensure CPI accurately reflects increases in inflation.
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