The Role of Discretionary Income in Charitable Giving

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PREFACE

Competition for donors has become a critical problem. It's not one of those Great Recession Problems, and it's not going to go away. And with expenditures increasing faster than public support for most organizations[1], there is particular focus on fundraising costs and the need to find efficiencies.

We are certain that building direct response fundraising programs in any medium based on discretionary income targeting offers break-through opportunity in both cost savings and returns-on-investments.

The syllogism is simple:

All giving is voluntary
All non-capital voluntary spending comes from discretionary income
All non-capital giving comes from discretionary income

It is true that in the nonprofit world motivational means and media of solicitation get perplexingly complicated. But the logic of this syllogism is nonetheless demonstrable. And that's what this paper is about.

The estimate of overall U.S. discretionary income in 2012 was $1.746 trillion. Varied research sources produce varied estimates of individual giving that would range from 11% to 13% of that $1.746 trillion. While unbridled growth of the nonprofit sector has made competition for donors something tantamount to a food fight in a prison cafeteria, the enormity of the source makes discretionary income a target worth calm contemplation and attention.

INTRODUCTION

Fundraisers and the agents they engage to get people to give to their institutions employ three means of persuasion: inspiration, enticement, and compulsion. Sometimes they employ all three at once. While the most successful at fundraising will concede that inspiration produces the best

[1] The Urban Institute's **The Nonprofit Almanac 2012** reported expenses for public charities increasing 53.2% for the decade 2000 to 2010 with public support increasing the lesser 41.2%

return on investment in building lasting relationships with donors, there's plenty of evidence in religious fundraising that compulsion works, and in many secular quarters that enticement – from address stickers to tote bags to DVDs of British soap operas to good seats at the theater – does as well.

But the giving is still voluntary and non-capital giving comes from discretionary income. Until very recently, we haven't had the resources we need to find who, in demographic terms, accounts for what quotient of discretionary income and how they spend it. The U.S. Bureau of Labor Statistics has collected and published income and expense data; it was researchers at New Strategist Press, LLC who took on the tasks of producing estimates of discretionary income and classifying expenses as discretionary in part or in whole.

Two publications from New Strategist Press are essential resources. One is **Who's Buying - Executive Summary of Household Spending - 8th Edition**, published last year, and the other is **American Incomes - Demographics of Who Has Money**, published this year. Both, along with other New Strategist resources can be found at www.newstrategist.com.

This paper relies heavily on New Strategist publications but provides only enough data from them to make the case for targeting donors on the basis of the demographics of discretionary income. The publications cited are heavy and worth their weight in gold. For detailed data, and specifically for reference to the methodology of determining discretionary income and expenses, we encourage adding the publications to one's library.

Further, **Who's Buying** is a comprehensive trove of information and data pertaining to commercial products and services, many of which also pertain to nonprofit organizations that are providing services for fees and products for sale that are related to their missions and programs.

DEMOGRAPHIC TARGETS

Good donor research, by which I mean sound methods enabling probability samples that ensure statistical reliability, have consistently shown age, education attainment, and household income – in that order – as prime predictors of giving.

Why is that?

The first answer (aha!) is that these demographics are very reliable predictors of discretionary income. Discretionary income begins to grow both as earnings increase and as financial obligations decline in either real or relative terms. Those things happen as people age, increasing substantially when people reach their mid-thirties, declining somewhat as they take on children's college bills, and then peaking between 55 and 64. While earnings decline after retirement and discretionary income drops on average for people over 65, the patterns of giving established earlier and exercised particularly during those peak income years tend to hold.

Discretionary income also increases, naturally, as a function of how well one is prepared for the workforce in terms of education attainment. The stark difference seen over the years between college graduate income and income of those who stopped at lower levels has moderated in recent years. But the incomes of those with professional and other graduate degrees continues to present that stark contrast.

But age and education produce more than just income, or the *capacity to give*. They play major roles in people's *disposition to give*. Age represents the continuum of life experience, and it along with education affect increasing disposition to selflessness, increasing curiosity, broadening awareness, and deepening social engagement.

While there has been much less research on disposition to give than there has been on capacity to give, what good research (again, the aforementioned qualification) has been done aligns with the experiences of fundraisers who've engaged in personal solicitations of donors. It is that experience that led me to a corollary definition of wealth for fundraising purposes: *wealth is having more money than you think you need.* Now I would amend that to say that wealth is having more *discretionary income* than you think you need.

Secondary reliable predictors of giving are the household presence of married/committed couples and, as Robert Putnam documented well in **Bowling Alone**, length of residence in the same community. Both those factors are predictors of community engagement and social capital and they, in turn, are predictors of volunteerism and philanthropy. But, length of community residence doesn't figure in either of the referenced data sources.

DISCRETIONARY INCOME TARGETS

Table 1 - Trends in Household Income

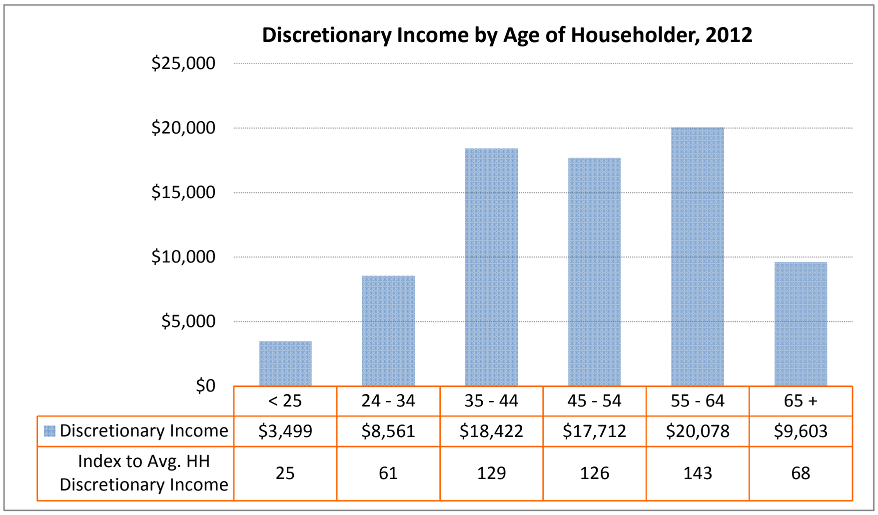
Trends in Household Income 2007 - 2012 **			
	2007	2012	% Change
Average household income	$69,862	$65,596	-6.1%
Discretionary income	$14,375	$14,037	-2.4%
Average Household spending	$54,965	$51,442	-6.4%
Discretionary spending	$11,740	$10,559	-10.1%

** in 2012 Dollars
Source: New Strategist based on BLS statistics

New Strategist defines discretionary income as "money that remains for spending (or saving or paying down debt) after one has paid for all the necessary costs of living a middle-class lifestyle."

Overall average household discretionary income in 2012 was $14,037. Through the tables and illustrations that follow, we have indexed discretionary income by various demographic segments to this average household number.

Illustration 1 - Discretionary Income by Age of Householder - 2012



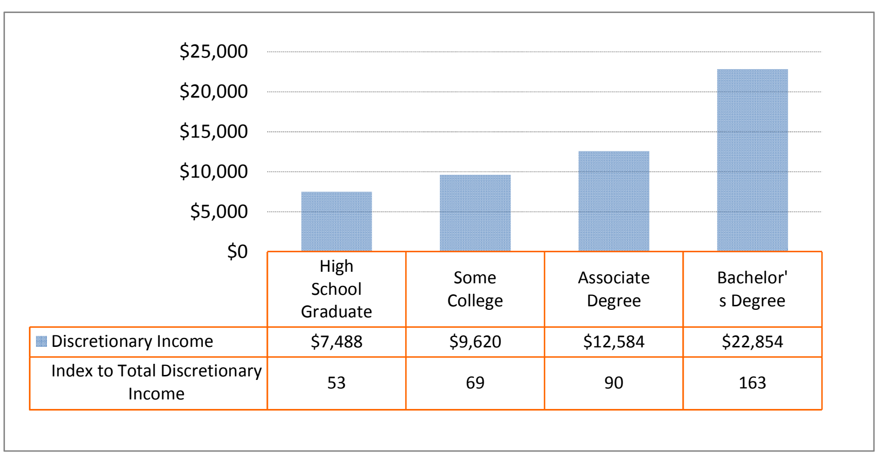
	< 25	24 - 34	35 - 44	45 - 54	55 - 64	65 +
Discretionary Income	$3,499	$8,561	$18,422	$17,712	$20,078	$9,603
Index to Avg. HH Discretionary Income	25	61	129	126	143	68

Age is the most reliable demographic indicator of the likelihood of giving, and discretionary income is the primary reason.

Earnings are the drivers of discretionary income and life stage bears on both earnings and expenses. So we see here that discretionary income jumps as people settle into careers and declines somewhat as children matriculate in colleges and universities. Donor research confined to income alone does not account well for the giving capacities of donors by age.

One thing the illustration tells us is that the value to fundraising of the market younger than 35 needs to be substantially discounted relative to returns that can be expected on investments.

Illustration 2 - Discretionary Income by Highest Educational Attainment of Any Householder - 2012



	High School Graduate	Some College	Associate Degree	Bachelor's Degree
Discretionary Income	$7,488	$9,620	$12,584	$22,854
Index to Total Discretionary Income	53	69	90	163

It's well known and documented that earnings potential is principally a function of educational attainment. So then is discretionary income. When we survey organizations' donors we always ask about their highest level of education and almost always also ask how much they have donated in the past year to institutions and organizations other than to political parties and their places of worship. The distinction between those with bachelor's degree and those having attained less education correlates with the pattern seen here; and the giving of those with professional and other advanced degrees reflects a similarly proportioned spread.

Table 2 - Discretionary Income by Household Income

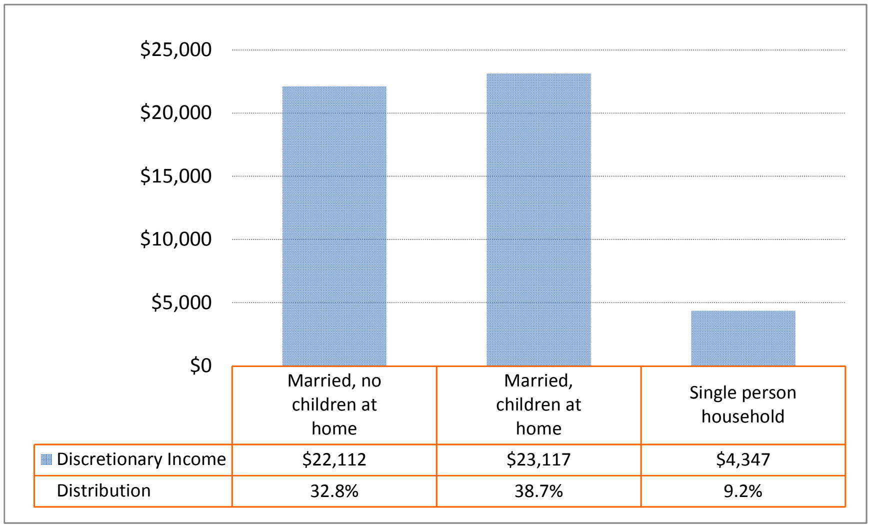
Discretionary Income by Household Income, 2012					
	Total Households		Avg. Before Tax Income	Discretionary Income	
	Number in '000s	% Distribution		Avg. Per HH	Distribution (Total is 100% of Aggregate)
Total Households	124,416	100.0%	$65,596	$14,037	100.0%
$40,000 - $49,999	11,010	8.8%	$44,759	$3,769	2.4%
$50,000 - $69,999	17,972	14.4%	$59,283	$8,458	8.7%
$70,000 - $79,999	6,946	5.6%	$74,689	$12,191	4.8%
$80,000 - $99,000	10,977	8.8%	$88,974	$16,870	10.6%
$100,000 or more	23,293	18.7%	$171,910	$55,082	73.5%

Source: New Strategist based on BLS 2013 Consumer Expenditure Survey

We've already seen the correlation of average household income to average household discretionary income. Here we can see where we should be targeting by household income when we are looking for donors or looking to increase the giving of donors we already have.[2] We have not included households with incomes less than $40,000 because, on average, they simply do not have discretionary income. It is a challenge to reckon with the fact that almost three-quarters of American household discretionary income is found in the 18.7% of households with income of $100,000 or more. One can almost feel the earth move as hundreds of thousands of fundraisers stop abruptly in their tracks!

[2] We're talking here are *fundraising* as opposed to marketing unsolicited *fund-giving* as most response to major disasters must be classified. The former has to do with managing return-on-investment while the latter is concerned with only the costs incidental to collecting and processing contributions.

Illustration 3 Discretionary Income by Type of Household, 2012



It's been known for a long time that two names on a donor record will invariably produce better response and higher gifts than one. For almost as long as we've known that, we have presumed it was simply a matter of increasing the odds of a communication getting through to one or the other donor or prospective donor.

But these data tell us something much different and more valuable. Households with married[3] couples, with or without children at home, have almost two-thirds more discretionary income than average.

DISCRETIONARY EXPENSES BY DONORS

New Strategist definitions of the spending categories of greatest interest to us – "Cash Contributions" in **Who's Buying** and "Cash Gifts" in **American Incomes** – are not as exacting as we would like them to be. The former includes some non-discretionary items like alimony, child support, and (arguably compulsory) support of children in college. The latter, while all discretionary, includes gifts to people outside the household.

Nevertheless, they include charitable contributions and, more importantly, since the data are based on a national household survey they include charitable contributions of all households, not just those whose tax returns itemize deductions. By way of ballpark reckoning, New Strategist has told us that their accounting for Cash Contributions in 2010 averaged $1,719 per household and that 79% of that amount ($1,358) is discretionary. IRS data for 2010 showed average

[3] The original data come from the Bureau of Labor Statistics Consumer Expenditures Survey. We assume they are using the term in its old conventional way. Our own research has found *committed couples,* by whatever term, contribute alike.

household deduction for contributions at $1,182[4]. The difference between the two numbers we can presume accounts for gifts other than those to nonprofit institutions.

Here from **American Incomes** is New Strategist's accounting of the top ten categories of discretionary expenditures in 2012.

Table 3 Top Ten Discretionary Expenditures in 2012

Top 10 Discretionary Expenditures in 2012		
	Avg. HH Spending	% of Total Discretionary Spending
1. Entertainment	$2,065.15	24.7%
2. Cash contributions to religious orgs.	$734.30	7.0%
3. Dinner at full service restaurants	$721.27	6.8%
4. Non payroll deposits to retirement plans	$582.46	5.5%
5. Cash gifts	$464.50	4.4%
6. Alcoholic beverages	$451.16	4.3%
7. Airline fares	$352.53	3.3%
8. Lodging on trips	$341.61	3.2%
9. Tobacco products and supplies	$331.72	3.1%
10. Lunch at full service restaurants	$300.91	2.9%

Source: New Strategist based on BLS Consumer Expenditure Survey

These ten items accounted for almost two-thirds of all discretionary expenditures in 2012, an accounting of shares that is not likely to change significantly year to year. Secular cash gifts, which include more than gifts to nonprofit institutions, accounted for 4.4% of discretionary expenditures.

For our purpose in targeting key donor demographics, we need to refer back to 2010 "Cash Contributions" accounted for by a multitude of demographic characteristics in **Who's Buying**. Here to remind us, from that publication's glossary, is the definition of Cash Contributions:

> *Includes cash contributed to persons or organizations outside the consumer unit, including court-ordered alimony, child support payments, support for college students, and contributions to religious, educational, charitable, or political organizations.*

Since we're using expenditure data for demographic targeting from 2010 as opposed to discretionary income data from 2012, and since the spending data includes non-discretionary items, we provide in the tables below cash contributions from **Who's Buying** for the principal donor demographics, indexed to 2010 average total household cash contributions.

[4] The contributions average per household for households itemizing deductions in 2011 was $4,434.

Table 4 - Cash Contributions by Age Indexed to Total Cash Contributions

Age Ranges	Index
<25	19
25 - 34	66
35 - 44	94
45 - 54	107
55 - 64	116
>65	139

Table 5 - Cash Contributions by Education Attainment Indexed to Total Cash Contributions]

Education	Index
No high school	54
High school grad	69
Some college/assoc.	93
Bachelor's degree or more	156

Table 6 - Cash Contributions by Household Income Indexed to Total Cash Contributions]

Ranges of HH Income	Index
$40,000 - $49,999	87
$50,000 - $69,999	98
$70,000 or more	176

Table 7 - Cash Contributions by Household Type Indexed to Total Cash Contributions

Household Type	Index
Married couples, no children	155
Married couples, children	108
Single person household	76

Source for all four is: Bureau of Labor Statistics 2010 Household Expenditures Survey; calculations by New Strategist

MAKING DISCRETIONARY EARNING AND SPENDING MEASURES COIN OF THE FUNDRAISING REALM

As an enterprise that is largely administered by process and media driven by service vendors, the difficulties of transforming broad-base fundraising to management by strategy based on data intelligence and analysis loom so large as to appear insurmountable. Targeting based on the demographics of discretionary income or expenditures, whether for new donors or for building value with those already acquired and retained is exactly the sort of data-based strategy required.

While increasingly dependent on the work of outside fundraising service vendors, the biggest challenges have the functional equivalency of wagging the dog. For the most part those vendors have captured scale in the economics of fundraising that cannot be approached by individual organizations of virtually any size. Indeed, as the principal funders of conferences and conventions, for the most part, they also capture the conversation!

Change and transformation are possible: the data will be supplied when its demand becomes evident.

For new-donor prospecting and acquisition, the positive development that points the way is the expanding presence of predictive modeling of massive cooperative donor bases. While each is reluctant to allow even their cooperating organizations to know much about their modeling, they are increasingly bringing external demographic and psychographic data to bear on their models. And there are more each day competing for business against each other and against conventional list brokers.

But gaining demographic data on discretionary income and expenditures for each organization’s donor value development strategies and programs will take longer because scale won’t come as readily for suppliers. It won’t begin to happen at all until organizations make common the practice of finding out those demographics of donors essential to gauging their giving value. Household income is hard to get directly from donors and can be inferred from geo-demographic data sources. But age, education attainment, household type, and length of residence can be gathered through well conceived and honed CRM practices.