

## The Arts Sector and the Current Financial Crisis (ARI)

*Cristina Fuentes La Roche* \*

**Theme:** The international financial crisis has had an impact on the arts sector and cultural organisations need to take measures to survive the economic downturn.

**Summary:** This paper explores current arts sponsorship trends in times of financial crisis. It looks at the private sponsorship sector, the public sector and at audience attendance in general. It puts forward a set of recommendations on what arts organisations can do to diversify their revenue models and to be less dependent on public and corporate support.

### Analysis:

#### *Financial Crisis: Effects on Private and Public Arts Funding*

The global financial crisis began in July 2007 was triggered by the dramatic fall in the value of securitised mortgages in the US on the back of the downturn in the housing market. These events gave rise to a global financial crisis and the collapse in confidence among banks and investors in the financial market. The resulting liquidity crisis prompted a substantial injection of capital into the financial markets by the US Federal Reserve, the Bank of England and the European Central Bank. The TED spread, an indicator of perceived credit risk in the general economy, spiked up in July 2007, remained volatile for a year and then spiked even higher in September 2008, when Lehman Brothers collapsed. This sent the world's stock markets into a tailspin, and a large number of banks, mortgage lenders and insurance companies either failed or were bailed out in the weeks that followed.

With the significant weakening of the financial sector and the slowdown in the economy, the economic downturn is affecting all sectors, including the arts and cultural sector.

Most arts organisations rely on a mixed-funding model, consisting of public money, private sponsorship and box-office or merchandise revenue. In continental Europe –in countries like Spain, Germany and France– arts organisations receive substantial subsidies from the government, contrary to the US, where private money, either corporate or from individuals, has always been the main funding channel for the arts.

In Spain the 1978 Constitution established a decentralised administrative structure on three levels: central government, regional government (with 17 regions and two

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\* *Director of the Hay Festival Cartagena de Indias and Programming Director of the Hay Festival Segovia.*

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autonomous cities) and local administrations (108 municipalities, plus provincial municipal councils and other local bodies).

In 2005, Spain's total public expenditure on culture at all three levels was of €5,144 million, approximately 0.56% of the Spanish GDP. Over the four-year period from 2000 to 2005, the total public expenditure on culture at all three levels increased, in nominal terms, by 62%. Most public cultural expenditure comes from local authorities (56.3%), followed by regions (28.5%) and finally the central government (15.2%). This shows the decentralised nature of the Spanish model, in which territorial authorities assume most of the responsibility for culture.

The financing of culture in the Federal Republic of Germany rests on several pillars. In keeping with the subsidiarity principle, culture –and thus its public financing– is first and foremost the responsibility of the citizens and their local communities. Only when the scope or nature of a cultural policy task is beyond the community's resources does the state step in as a sponsor. The municipalities thus bear the lion's share of the cost of financing public cultural activities and institutions, followed by the Länder. Government expenditure on culture totalled €8,322 million in 2007.

In 2002, French public financing for culture totalled €6 billion, including €2.6 billion for the Ministry of Culture and Communication and €3.6 billion for the other ministries. In Metropolitan France, the cultural expenditure of the local authorities is at a similar level: €4.1 billion for municipalities of more than 10,000 inhabitants, €280 million for publicly-owned establishments of inter-municipal co-operation (with the possibility of raising the tax), €1.1 billion for the *départements* and €360 million for the *régions* (figures from 'Compendium – Cultural Policies and Trends in Europe').

In the US the situation is completely different, The National Endowment for the Arts (NEA), a public agency dedicated to supporting excellence in the arts, is the largest public funder, with a budget of US\$155 million in 2009. However, this is less than 1% percent of total arts philanthropy in the US and only a small fraction of the art and culture funding provided by many of the European governments. In 2005, the US private sector gave US\$13.51 billion to support the arts throughout America (according to 'Americans for the Arts National Arts Policy Roundtable Publication Report 2006').

#### *Private Sponsorship*

With the corporate and financial sector under severe pressure to cut costs, and with major changes in top management, arts related sponsorships and support have come under closer scrutiny. The arts sector could become an easy victim, especially in circumstances when arts sponsorship and support is the result of a Chairman's whim or is mainly used as an instrument for corporate entertainment.

While the arts in continental Europe rely heavily on public support, the UK has always been somewhere in between, largely dependent on a mixed funding model.

In the UK, according to the respondents of the 'Arts & Business Private Investment in Culture Survey', private investment (PI) in 2007-2008 accounted for an average of 13% of cultural organisations' total income. Public sector funding, including funding from the arts councils, the UK Ministries of Culture, other governmental departments, local authorities, other public subsidies and lottery funding, made up 54% of the total income of cultural

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organisations. The remaining 33% was raised through earned income, including ticket sales and trading.

Research by Arts and Business shows that 30% of the corporate donors who gave more than £1 million to the arts last year expect these budgets to shrink. Respondents also felt it was arts sponsorship that was most vulnerable, compared with charities and sport. Many companies with established records in the arts fear being criticised by angry shareholders and puzzled customers. 'The big sponsorship companies that we deal with are very sensitive to the fact that they don't want to be seen as frivolous', said Natalie Melton of Arts and Business.

A survey commissioned by Arts & Business in April 2009 ('Market Trends' by Tina Mermiri) shows that smaller arts organisations are already feeling the pinch in terms of securing external funding (from the public, particularly local authorities, but also in the form of private investment, particularly business investment). Most arts respondents (63%) are already experiencing a substantial decrease in business investment.

Individual giving is on the whole faring better than business investment, with membership subscriptions for most organisations being maintained (if not increased). Funding from trusts and foundations is also difficult to secure, as expressed by more than half of the arts respondents.

However, most organisations think that the demand for their services will increase although it will be harder for them to continue providing quality content to the extent that they did previously.

As the majority of small arts organisations are finding it difficult to secure external funding (especially from private sources), they are keen to become more flexible and creative, coming up with alternative means of raising funds to help them survive.

Businesses still consider 2009 a critical year, with confidence levels lower in April 2009 than in November and August 2008. However, they are now more confident about their future investment in the arts, with 87% of respondents expecting to invest more (often) in the arts by 2011, although the discernible trends seem to show that businesses will prefer to invest in more projects rather than in larger projects.

This seems to match the anecdotal evidence that badge/blockbuster sponsorships will decrease in popularity, as will corporate hospitality and flashy events.

Business priorities are shifting in terms of the kind of investment they want to make in the arts. Staff engagement is becoming increasingly important, in light of business needs to keep staff morale high. Marketing is still important, and so is corporate social responsibility.

#### *Public Funding of the Arts*

Public funding of the arts is under threat as government budget deficit is rapidly increasing, on the back of slowing economies and the credit crisis.

The arts sector has experienced public funding cuts: in the UK, the Arts Council has cut its budget by £4 million for 2009, while Italy's arts fund, the FUS, has reduced its budget from a projected US\$726 million to US\$509 million (according to AGIS, the entertainment

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trade organisation that liaises with the government). However, at the same time governments have created 'recovery funds' to preserve the sector.

On 10 April 2009 the US National Endowment for the Arts announced US\$19.8 million in one-time grants under the American Recovery and Reinvestment Act of 2009 (Recovery Act). The grants are aimed at the state arts agencies and regional arts organisations to support the arts sector of the economy. Potential recipients include organisations in the performing, visual and literary arts and all applicants must be previous NEA award recipients sometime in the previous four years).

Grants are limited to salary support, full or partial, for one or more positions that are critical to an organisation's artistic mission and that are in jeopardy or have been eliminated as a result of the current economic climate, and also for fees for previously engaged artists and/or contractual personnel to maintain or expand the period during which such persons would be engaged.

In April 2009 the Arts Council England introduced an immediate £4 million cut in its budget, but announced a further £40 million 'Sustain fund' for arts organisations suffering because of the economic downturn. The 'Sustain fund' will be available over the next two years (or until the money is spent) and will award grants of between £75,000 and £3 million to arts organisations severely affected by the recession. Its aim is to offer a rapid response, with no more than a six-week delay between application and decision.

The size of the grants and the fact that individual artists are excluded (they are being directed towards Grants for the Arts, which has recorded a £2 million rise since last year, to £54 million) suggests that it is the big buildings that are most likely to benefit.

However, the Chairman of Arts Council England, Dame Liz Forgan, warned: 'This is not about money for rocky organisations. This is about successful organisations whose operations are threatened specifically by the recession, for example banks stopping their credit'.

It was also for groups who are doing 'excellent and brave and ambitious' work, she said. 'Audiences have been developing over the last 10 years and there is a complete appetite for the ambitious and for the new. It would be wrong for arts groups to retreat into safety, leaving audiences bored and disheartened'.

In Spain the newly appointed Minister of Culture has announced €22 million in support of the cultural sector and creative industries that will also have a fixed interest of no more than 2% from TAE (equivalent annual fee or *tasa anual equivalente*).

Hence, although traditional public arts funding is on the decrease, new types of 'recovery' funds have become available for arts organisations undergoing financial difficulties, thereby shielding them from some of the negative impact of the recession.

#### *Box Office Revenue/Merchandise*

When it is impossible to change what is happening to one's financial health, the need for personal health and wellbeing is heightened. The arts sector is to some extent 'recession-resistant' as people seek 'well-being' by spending more time at a museum, attending or taking part in sports, or escaping to the theatre, ballet or concerts. The public benefit from the 'feel-good' factor provided by smaller luxuries as a respite from the world of global

credit crunches and negative equity, rather than spending their money on major items like overseas travel or new cars. In difficult times, history proves that the theatre, cosmetics (the 'lipstick test') and music sales tend to boom, as arts and creativity flourish.

The success of *Mamma Mia!* is just one example of how the arts can thrive in times of crisis. The Abba Economic Index, a little-known financial measure with an uncanny correlation to tough times, is on the up again. It first entered a bull phase in the mid-1970s, when the band rocketed to stardom amid the three-day week and raging inflation. The UK was an economic basket case, yet ABBA was a huge success.

When recession struck in the early 1990s, we found solace in *Abba Gold: Greatest Hits*, which was released in 1992. It topped the UK charts. The latest Abba-fest will help Hollywood defy the recessionary gloom. The film factory's box office take for June 2008 was up 17.3% over the same month of the previous year.

The latest edition of the The Hay Festival of Literature, in May 2009, saw a record number of visitors, with a 20% increase from the previous year. 'People want to see what others have got to say about the recession', said the festival Director, Peter Florence. 'What we are seeing is the evening entertainment tickets are selling very, very well, on one hand, people want to get away from the recession and enjoy themselves, then on the other hand, we are selling out of tickets to the economic events'. Audiences were keen to find answers from Howard Davies, the LSE's Director who talked about the Global Crisis, Niall Ferguson, author of *The Ascent of Money*, and Amartya Sen, the Economy Nobel prize winner.

Indeed, recessions often bring about a flowering of the arts. Jazz prospered in America in the Great Depression in the 1930s as people stayed in and listened to their radios.

In Spain the book and publishing sector are resisting the crisis. Antonio María Avila, the Director of the Spanish Publishers' Association, says that books sales have not seen a significant change: when things are going well sales do not increase dramatically, but neither do they fall drastically in times of crisis. Even though, according to Pilar Gallego (President of the Madrid Book Fair), book sales dropped between 15% and 20% in the first half of the year, the Madrid Book Fair recorded a 10% increase in sales compared with 2008, according to its Director, Teodoro Sacristán.

According to the Generalitat, the International Music Festival in Benicassim programmed for July 2009 is expecting 200,000 visitors this year, a 35% increase compared with 2008. According to the organisers, the pre-booking of tickets has set a record, with all tickets having been sold out.

Theatre visits in Spain are also on the increase. Daniel Martínez, director of FOCUS group, said that audiences last year had increased by 20% thanks to musicals, while attendance in alternative theatre venues was up 3%. In 2008 mainstream theatres had a total audience of 2.6 million, 400,000 more than in 2007.

According to the economist José María Álvarez de Lara, Spain's cultural industries in general have recorded annual increases of 3%-4% and, although growth is likely to slow down, it should still expand by around 0.5%-1%.

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### *What Can Arts Organisations Do?*

Against a backdrop of mounting challenges, there is still quite a lot that can be done. The main point is that the non-profit sector must be proactive and inventive when responding to a downturn. How can it take advantage of the current crisis and be better prepared for the future? These are some recent developments:

- (1) **Exploring financial innovations/solutions.** Capital has become a scarce resource for many arts organisations, having tied up most of their capital in fixed assets such as buildings and properties, art collections, etc. A number of financial innovations, such as borrowing against an arts organisation's art collection, are emerging. Two specialist New York financial institutions –Art Capital and Art Finance Partners– are providing finance to museums and other arts institutions that are in the position to put up works of art as collateral. Many of these are facing significant cuts in endowments after a drop in private donations. The most prominent example is the Metropolitan Opera, that decided to put up its celebrated Chagall murals as part of the collateral for an existing loan it had with JP Morgan. This enabled it to free-up cash, currently used as collateral for the loan. Structured finance, such as the securitisation of future box-office income, and lease buy-back schemes on properties owned by arts organisations are other possible means of releasing cash for operations.
- (2) **Maximising brand value through merchandise.** Culture and art is becoming a valuable commodity in our society. Arts brands, such as Tate, V&A, El Prado, MoMA, Guggenheim and Louvre have become highly valuable brand names. Whilst Guggenheim and Louvre have explored their brand value through global franchises, others are using their brands for merchandising. Merchandise has become one of the most important sources of revenue for many arts organisations. The Tate recorded a turnover of £13.4 million in 2007-08 from merchandise, generating a profit of more than £2 million. A newly created company in the UK – CultureLabel.com– aims to help arts organisations maximise the revenue from cultural merchandise. CultureLabel.com is a unique new retail project bringing together the best global culture brands. The website will act as a portal for 'cultural' merchandise from museums, galleries and festivals and could enhance and facilitate new revenue streams for these organisations.
- (3) **Developing a membership base that can be mobilised politically for advocacy purposes as well as economically for resource generation.** This can be done through a traditional membership scheme, with members receiving certain privileges like preferential bookings, previews and newsletters. Most arts organisations are actively cultivating their members through tiered membership schemes. Museums like the Tate have created a number of 'acquisition committees', such as the Latin American Acquisitions Committee, which aims to support the purchasing of works of Latin American art. These committees are 'exclusive clubs' for people who wish to contribute financially to building up the Tate's art collection.

Outside the museum world, other innovations are taking place. V22, a London-based art company, was established in 2006 and listed on one of London's smaller stock exchanges. The arts fund has 100 collectors and 28 artists as shareholders. Advisers include David Thorp, formerly Director of the South London Gallery, and Thomas Rowland, formerly at the Saatchi Collection. The fund specialises in works by young

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artists like Marcus Harvey, Harland Miller and Peter Jones, who are represented by good dealers or have some of their work in major collections (the artists become shareholders and so benefit from any profits). The investor puts up £20,000 (for 800,000 shares) and gains tax relief because it qualifies as an SIPP (self-invested personal pension). For the investors this means an 'angel' relationship with artists they like and a modest return on an investment, while the artists gain cash flow without generating financial debt. This model could be a way for arts organisations to attract 'angel' investors.

**Conclusion:** Arts organisations are facing global economic hardship. By reviewing their funding policies, this paper argues that new funding patterns and business models are likely to emerge from the current economic crisis.

In January 2009, Helmut K Anheier from the University of Heidelberg argued in a paper on the global economic downturn that: '... the crisis offers perhaps as much in terms of opportunities as it does in terms of challenges. It will lead to the demise of some nonprofits and the rise of others, some will flourish and others become less relevant, moribund, and defunct and may even disappear altogether'.<sup>1</sup>

Surviving the economic downturn requires a pro-active stance on behalf of arts organisations, who are already responding to the crisis by being innovative in the way they think about their assets, their business and their brands. Ultimately, creativity, one of the sector's intrinsic features, is likely to be its best asset.

*Cristina Fuentes La Roche*

*Director of the Hay Festival Cartagena de Indias and Programming Director of the Hay Festival Segovia*

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<sup>1</sup> Helmut K. Anheier (2009), *The Global Economic Downturn, Philanthropy and Nonprofits - Reflections on What it Means, and What To Do*, Centre for Social Investment, University of Heidelberg, & Center for Civil Society, UCLA, January.