

## *Cross-National Variations in the Importance of the Non-Profit Sector*

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UDK: 061.2.01  
330:061.2

Izvorni znanstveni rad (original scientific paper)

Primljeno: 28. 10. 2010.

Prihvaćeno: 18. 3. 2011.

This paper empirically investigates various factors affecting the variations in the size of the non-profit sector using a cross-country data in the sample of selected countries. Namely, the available data on sector employment (workforce) indicate substantial variations in the size of the sector among countries, although certain problems exist with measurement of the sector size, mostly related to its diversity. The existing literature can provide several theories, hypotheses and concepts that could potentially help to explain those differences, those approaches ranging from economic, political, social, organisational, and even interdisciplinary ones; the outcome of those approaches is the extrapolation of various factors that affect differences. The research approach taken in the paper is focused on combining the effect of those factors for the purpose of their empirical verification. The results indicate that supply side

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factors tend to be more important in explaining differences in the size of the sector among countries.

*Key words:* non-profit economy, size of the non-profit sector, sector labels, cross-country variations, demand and supply side factors, empirical analysis

## 1. Introduction

The non-profit sector includes a diverse set of organisations, which basically serve common purposes, such as organisations in health, human services, arts, culture, education, research, religious services, fund-raising and advocacy activities etc.<sup>1</sup> The main cause for the existence of the non-profit sector is the provision of certain public, or more precisely, quasi-public or common goods and services, which means that non-profit sector is technically not part of the government sector. Namely, the non-profit sector activities rely primarily on the ideas of individualism and pluralism, rather than on ideas of equality and justice, which are prevailing in the government sector. This means that, in practice, the non-profit organisations try to avoid delivering universal and compulsory public goods and services as does the government sector, but rather those quasi-public goods and services that are determined by the willingness of individuals, businesses, governments, and other institutions to cooperate with non-profit organisations for the purpose of their mission and goals achievement (Hodginkson and Weitzman, 1996).

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<sup>1</sup> The data presented in the John Hopkins Comparative Nonprofit Sector Project (2004) have revealed that, on average, two-thirds of all non-profit paid employment is concentrated in education, health, and social services, which are classical welfare services. Corry (2010) has pointed out that this sector in practice includes non-governmental organisations (NGO's), charities, self-help groups, social enterprises, clubs, and networks. Similarly, Kumar (2010) has stressed, following case-study approach, potentially different »institutional and mobilisation forms« of non-profit sector, such as, e.g., development-centric non-governmental organisations (NGO's), community-based organisations, cooperatives, philanthropic organisations, social movements etc. Thus, this means that non-profit sector does not include only non-governmental organisations (Salamon, 2010), although the terms may often be used as synonyms and be potentially confusing (see also chapter 2 on terminology). Notwithstanding, there are also diverse organisational forms of organisations in the sector such as associations, institutes, unions, foundations etc.

The non-profit sector emerged due to several different forces: the existence of both market and government failure<sup>2</sup> in the provision of certain goods and services to citizens, the emergence of pluralism and individual freedom in modern societies, and the increased pressures on solidarity among people (see readings in Ott, 2001). This means that the existence of the non-profit sector is, in fact, the result of the development of democratic society and the capitalist economic system. Consequently, the existing literature and empirical evidence both generally support the thesis that there has been a substantial growth in the number of non-profit organisations and in socio-economic importance of the non-profit sector in recent decades (see Salamon, 1994; Weisbrod, 1998; Hammack, 2001 etc.).<sup>3</sup> Nevertheless, substantial variations exist in the size of the non-profit sector across countries. Consequently, the main purpose of the paper is to identify and empirically validate potential factors that shape the differences in the size of the non-profit sector in the sample of 38 countries for which the data on the size of the sector could be obtained. The paper is organised as follows: chapter 2 presents definitions and functioning principles of the sector; chapter 3 delivers an insight into socio-economic importance of the sector; chapter 4 describes theories on non-profit sector growth and development; chapter 5 delivers an overview of the existing research on the size of the non-profit sector, whereas chapters 6 and 7 present data, methodology and findings of empirical analysis on the cross-country variations in the sector size; finally, paper concludes with brief concluding remarks and list of references.

## 2. The definition and functioning principles of the non-profit sector

Salamon and Anheier (1997) have defined the non-profit sector as collection of entities/organisations that have five characteristics: institutionalisation, separation from government, self-governance, non-profit distribution and certain degree of voluntarism. This structural-operational definition

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<sup>2</sup> Intuitively, it can be concluded that in economic downturn both market and government failures increase, indicating that the relative socio-economic importance of the non-profit sector should increase.

<sup>3</sup> Salamon et al. (2007) have reported that these organisations should, on average, account for approximately 5 % of GDP.

particularly emphasises non-governmental and independent nature of non-profit sector organisations.<sup>4</sup> The status and importance of this sector are influenced by various factors, such as the state of domestic economy and public policies, changes in population preferences etc., but unique to this sector are certain sources of support, which are based on voluntary donations of time and other contributions (Hodgkinson and Weitzman, 1996).

Indeed, Salamon et al. (2007) have revealed a distinctive economic structure of the sector, such as substantial labour insensitivity and mobilisation of volunteer effort. This means that functioning of the sector is based on the existence of so-called economies of grants, which include voluntary donation of time, money and other resources, which enables the sector to operate in almost all areas of social life, often quite independently of the current political and economic conditions (Ott, 2001). Namely, the essence of the non-profit sector is that it receives operating resources from many different sources, primarily from donations, governmental funding and market activities. Nevertheless, recently observed trends, which can also be elaborated from the data extracted from the John Hopkins Comparative Nonprofit Sector Project (2004), have revealed that user fees and other sources from commercial activities are, on average, increasingly replacing governmental funding that prevailed in last few decades, while private philanthropy has become relatively quite negligible.<sup>5</sup> This has occurred predominantly due to the significant pressures for larger commercialisation of the activities of non-profit organisations in recent decades, which have been caused predominantly by changes in the system and the amount of budgetary and grant financing.

Since this is a very diverse sector, numerous alternative terms for defining it are used both in theory and in practice. For instance, this sector is often named as a third, independent,<sup>6</sup> voluntary or charitable sector, although

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<sup>4</sup> See also Handbook on Non-Profit Institutions in the System of National Accounts (2003).

<sup>5</sup> If the value of volunteer work is taken into account, the relative importance of private philanthropy increases, although it is still smaller than value of user fees and governmental financing. Nevertheless, substantial cross country variations exist also in the relative importance of different types of financing. Specifically, user fees tend to prevail in Latin America and Eastern Europe according to the John Hopkins Comparative Nonprofit Sector Project findings, whereas government funding tends to be the most important source of revenue in Western Europe. More on this see also Salamon et al. (2007).

<sup>6</sup> The term independent should describe the ability to implement certain social goals and missions without being inhibited by the need for achieving economic efficiency or gaining political support (Ott, 2001).

the latter three labels actually do not reflect present day reality in this sector (Worth, 2009). Namely, this sector is actually very dependent on the sources derived from the government, business and private donations, as well as, increasingly, from market activities. Similarly, the labels voluntary and charitable define the sector as the one depending on voluntarism and being charitable in nature, which are not the most important modus operandi of the sector. Finally, another commonly used label for this sector is civil society, which is, according to the Civicus (2006) definition, »the arena, outside of the family, the state, and the market where people associate to advance common interests«.

Indeed, Lorentzen (2010) has recognised that four most commonly used labels for this sector are non-profit, third, voluntary and civil sector (society). He has admitted though that the choice of the sector label seems to be accidental, which means that labels are usually used as synonyms. He has argued that voluntary label was the first one to emerge as the result of the ideological struggle between associations and the state in the times of industrialisation in the nineteenth century. Nevertheless, all three other most commonly used labels emerged much later. For instance, third sector label emerged in the 1970s as the sector was seen as potential alternative to the expanding state and market-based welfare. In contrast, civil society label gained ground in the 1980s as this sector was associated with new evolutionism and the need for an autonomous civil sphere outside the state, which was particularly relevant in totalitarian regimes as well as in circumstances of state-controlled reforms. Similarly, non-profit label also gained ground in 1980s, describing the sector as the one with existing non-distribution constraints and differentiated demand, which served as the form of distinction from government and business (for-profit) sectors.<sup>7</sup> In particular, Lewis (2010) has summarised that these »over-lapping« labels mainly reflect different cultures and histories in which thinking of the sector emerged. Specifically, he has argued that the label non-profit tends to be more rigorously used in the United States, where the market is dominant, whereas label voluntary tends to be more rigorously used in the United Kingdom, where longer tradition of voluntary work exists following development of charity law. Interestingly, the author has also pointed out that acronym non-governmental is often taken as synonym to non-profit, particularly often used in relation to in-

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<sup>7</sup> Nevertheless, although several labels exist, often used as synonyms, the paper uses the label non-profit, which is more often used in economic and political literature.

ternational and developing country activities, although these two labels should not mark the same thing.<sup>8</sup>

### 3. The socio-economic importance of the non-profit sector

The non-profit sector currently represents an important part of economical, political and social environment of almost all developed countries. In particular, the growth in socio-economic importance of the sector has been very intensive in the last few decades. Salamon (1994) has labelled that process as »associational revolution«. He has stressed that this growth occurred because non-profit sector actually increasingly complements government and markets in the provision of important services, especially in health, education and social fields. Since those services are often funded or subsidised by government, this means that government indirectly promotes the growing importance of non-profit organisations in the economy. Some authors (see, e.g. Anheier, 2000) have even argued that actually the introduction of the New Public Management initiative, which among others promoted the ideas of »lean government« with privatisation and commercialisation of certain governmental functions, contributed to the growth of the non-profit sector.

Weisbrod (1998) has also pointed out that the trend of growth in scale and scope of the non-profit sector exists, although he has stressed that the main reason for the growth is to be found in rising heterogeneity of population, caused by larger human migrations and information flows. Namely, increased heterogeneity of modern societies causes that the preferences and needs of citizens differ more and more, which decreases the demand for universal public goods and services and increases the demand for »quasi-public« goods and services with more individualistic and pluralistic characteristics.<sup>9</sup> Similarly, Hammack (2001) has also observed the

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<sup>8</sup> Namely, the United Nations tended to label certain international non-state organisations with consultative status in the UN activities as NGO's. See also Salamon (2010) on this issue.

<sup>9</sup> In this context, the relationship between welfare state retrenchment and the role of the non-profit sector should be particularly interesting. Namely, the evidence exists for supporting the thesis that voters will find the redistribution policies, which can mainly be observed in the amount of government transfer spending, more appealing in socially more homogeneous societies (see e.g., Alesina, Glaeser and Sacerdote, 2001). This should impose certain implicit restrictions on the further development of welfare state and its expansion, which is not related to the prevailing fiscal limitations; increased social fractionalisation, which has characterised

same trend. However, he has argued that this growth had occurred as »quiet revolution«, not due to the private charitable giving and volunteering, but predominantly because individuals, businesses and other institutions had gained greater independence from the government. Besides, increased incomes of the individuals and families had allowed them to increase demand on the educational, health care, cultural and social services that non-profit organisations tend to provide.

As described above, the existing literature generally supports the thesis that there has been a growth in the size of the non-profit sector in recent decades, even if different measures of the size are used.<sup>10</sup> Nevertheless, substantial differences exist in the development and relative socio-economic importance of the non-profit sector among countries, even among the developed ones. This can also be extracted from the existing cross-national data on the size of the non-profit sector published in the John Hopkins Comparative Nonprofit Sector Project (2004).<sup>11</sup> For instance, as it can be observed from Table 1, the size of the non-profit sector, if measured with the share of its workforce in economically active population, seems to be larger in some Western and Northern European countries as well as in Anglo-Saxon countries. In contrast, the activities of non-profit organizations are usually hampered in totalitarian political regimes, as there exists a tendency of the political system and government to dominate civil society. For instance, this experience can be observed in post-socialist countries or in some Asian and African countries, where the size of the non-profit sector is still relatively smaller than in compared industrial countries. In particular, Civicus (2006) has reported that in post-socialist countries one of the major factors affecting smaller extent of non-profit economy is the legacy of socialism, as rather negative attitude towards voluntary work has been observed in those countries. The argument is

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the majority of developed countries in recent years, obviously affects political process and decreases preferences for any extensive formulation and implementation of certain social policies. Since this dynamic will obviously dominate in the future, further limitations on welfare state development and expansion are to be expected. This means that the functions of welfare state should become increasingly the domain of non-profit organisations, but also in part the domain of the for-profit organisations, mainly in the form of socially responsible activities.

<sup>10</sup> It should be noted that the size of the non-profit sector is usually measured with sector employment, expenditure and revenue size, extent of volunteering, membership, number of entities etc. It needs to be stressed that economic approaches typically concentrate on the extent of employment in the sector, its revenues or expenditures (see Anheier, 2000).

<sup>11</sup> It should be stressed that the lack of internationally comparable data exists, which can be attributed to large diversity of activities that non-profit organisations perform and large diversity of organisational forms of non-profit organisations.

that the citizens in those countries strongly associate this type of work with the socialist era, during which people were often ‘coerced into volunteering’ for state-controlled organisations.<sup>12</sup>

Table 1: Size of the non-profit sector (sector workforce) in selected countries<sup>13</sup>

Country	Workforce (% of economically active population)	Country	Workforce (% of economically active population)
Argentina	4,8	Japan	4,2
Australia	6,3	Kenya	2,1
Austria	4,9	Mexico	0,4
Belgium	10,9	Morocco	1,5
Brazil	1,6	Netherlands	14,4
Canada	12,1	Norway	7,2
Chile	5,2	Pakistan	1,0
Colombia	2,4	Peru	2,5
Czech Rep.	2,0	Philippines	1,9
Denmark	6,8	Poland	0,8
Egypt	2,8	Portugal	4,2
Finland	5,3	Romania	0,8
France	7,6	Slovakia	0,8
Germany	5,9	South Africa	3,4
Hungary	1,1	South Korea	2,4
India	1,4	Spain	4,3
Ireland	10,4	Sweden	7,1
Israel	8,0	Unit. Kingdom	8,5
Italy	3,8	United States	9,8

Source: The John Hopkins Comparative Non-profit Sector Project (2004)

<sup>12</sup> See, e.g., Brhlikova (2004), Svitkova (2004) or Giving in Europe (2009) on the development of the non-profit sector in post-socialist countries.

<sup>13</sup> The data for the share of non-profit sector in economically active population exclude religious worship organisations. The data refer to the collecting period of 1995-2000, except for Portugal (2000), Canada (2003), Chile and Denmark (2004). See the source for the data and methodological references.

Finally, it should be acknowledged that various alternative measures of the size of the non-profit sector exist, predominantly in the form of various indexes (e.g., Civicus Civil Society Index (Diamond) – CSI, Global Civil Society Index – GCSI, etc.). Several authors have acknowledged that certain limitations to such measurement exist. For instance, Lyons (2009) has argued that GCSI measures only associational life, but does not measure other two dimensions of the sector, that is good society and public sphere, although it is formally more rigorous than CSI. In contrast, CSI is broader, but relies more on judgements of groups of individuals potentially representing or having knowledge on the state of the sector in particular country. In this context, Heinrich (2005) proposed two dimensions for measurement of the sector size: (1) structural dimension, which should capture individual actions and organisational presence in the sector; and (2) cultural dimension, which should capture both the public sphere and good society in the sector, describing the amount of plurality of social norms that exist in the sector. Moreover, one of the problems associated with using those alternative measures is that they tend to be developed for specific sets or groups of countries, thereby omitting the usage of alternative measures in the analyses performed in the same sample of countries.<sup>14</sup>

#### 4. The non-profit sector growth and development theories

Theories on the development and growth of the non-profit sector are multidisciplinary and interdisciplinary in their nature, since they have been developed by economists, political scientists, psychologists, sociologists, historians etc. This has caused that there is no unified theory, which would be able to explain the existence, but also the differences in the development of the non-profit sector across countries (Worth, 2009). Two distinct approaches exist in the literature, one being more focused on explaining the growth of the non-profit sector in time, and the other being on explaining the differences in the size and development of the non-profit sector within and among different societies. Some common

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<sup>14</sup> For instance, in the sample of analysed 38 countries, GCSI provides data only for 20 them.

features of both approaches exist, although the discussion below focuses more on the hypotheses, concepts and theories that are trying to address potential factors affecting differences in the size of the non-profit sector between countries, which can be observed in Table 1.

The existing hypotheses, concepts and theories on the differences in the size and development of the non-profit sector can be separated as demand side and supply side approaches. The demand side approaches usually focus on the role of the non-profit sector in provision of goods and services that are not adequately provided by the for-profit and government sectors. In contrast, supply side approaches usually contemplate that size of the non-profit sector is related to the extent of resources available to the sector, which should, among others, also depend on the wealth of certain society (Grønbjerg and Paarlberg, 2001). It is worth noting that supply side oriented approaches emerged later, as demand side hypotheses often provided inconclusive statements on the reasons for the non-profit sector existence. Both approaches extract micro and macro factors that shape the differences in size of the non-profit sector, but given the purpose of the paper, the discussion presented below is more focused on identifying potential macro factors affecting differences, since they can also be empirically verified.

Among typical demand side oriented approaches, failure theories are one of the most influential ones. These theories are rather economic in their nature; they state that the non-profit sector exists due to market failure, contract failure, and government failure (Young, 1998). According to the market failure argument, the need for the non-profit sector emerges in order to offset transaction costs, typical example being the costs of obtaining information or costs of pooling the resources to achieve common goals etc. Similarly, contract failure argument supplements the idea of market failure argument in the case of complex goods (i.e., higher education, medical treatment etc.), where consumers are unable to competently evaluate the quality and quantity of services they are receiving. This argument extends transaction costs to informational asymmetries.<sup>15</sup> Finally,

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<sup>15</sup> Market and contract failure arguments are sometimes labelled as trust theory (see Hansmann, 1996; Anheier, 2000). Namely, imperfections in market relationship and informational asymmetry can cause that providers are able to exploit market position and ignorance of buyers to maximise their interest (Grønbjerg, 1998). In this sense, because non-profit sector organisations have less incentives and possibilities to exploit buyers' ignorance, they are usually more trusted in providing certain goods and services, which are characterised by large market imperfections or the existence of important informational asymmetries (e.g., education, counselling etc.).

government failure argument contemplates that the need for non-profit sector emerges, when governments fail to correct market failures, thereby making the space for non-profit organisations to fulfil the unsatisfied needs. There are usually certain political and structural reasons exist that prevent government from fulfilling the unsatisfied needs; one of them is the nature of government to respond to the needs and demands of majority. This means that in diverse societies there is the problem of achieving universal agreement on goods and services provided by government.<sup>16</sup>

Hence, government failure argument has been also addressed in heterogeneity theory (see Weisbrod, 1998), which argues that the relative importance of the non-profit sector is related to the increased heterogeneity of modern societies. Namely, heterogeneity causes increased differences in citizens' needs and preferences, thereby decreasing demand for universal public goods and services but increasing demand for "public" goods and services with more individualistic and pluralistic characteristics. The conclusion is that countries with more homogeneous demand should have a relatively smaller non-profit sector than the countries with more heterogeneous demand.

However, the existing literature stresses that it is necessary to differentiate between the two distinct features of heterogeneity: socio-economic (supply side) heterogeneity and cultural (demand side) heterogeneity. Cultural aspect of heterogeneity is actually in line with Weisbrod's proposition of the positive affect of heterogeneity on the size of the non-profit sector due to the larger demand for products and services with more individualistic and pluralistic characteristics, which tend to be provided by non-profit organisations rather than by government. The cultural heterogeneity of society could be described with ethnic, linguistic and religious fragmentation of population. In contrast, the effect of socio-economic heterogeneity on the size of the non-profit sector should be opposite. The idea is that the resources available for non-profit organisations are more easily attainable in more socially homogeneous societies, where there is

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<sup>16</sup> It is worth noting that theory of the commons (Lohmann, 1992), an interdisciplinary approach to non-profit sector analysis, actually contradicts failure theories. Namely, this theory argues that non-profit sector actually produces common goods, which are goods that, unlike private goods, cannot be consumed by individuals, but they also do not, unlike public goods, benefit to all people. These goods actually benefit to all members of the particular commons but not to those beyond. This theory actually states that non-profit organisations do not make up failures of market or government, but they produce a third kind of goods (common goods). More on the analysis and description of common goods see Worth (2009).

also larger social cohesion, as the frequency of social interactions tends to be greater in more socially equal societies (Corbin, 1999). Furthermore, the existing research suggests that the most suitable measure of socio-economic heterogeneity of society is income inequality (usually measured with Gini index).

Government failure argument has also been addressed in political theories of the non-profit sector, although variation has emerged as political limitations to government provision of products and services have been introduced in those theories. Namely, political theories have stressed that non-profit sector activities could be viewed as private form of public policy implementation, since governmental policy making and implementation tend to be subjected to the constraint of political feasibility, which is not the case in non-profit sector (Douglas, 1987). In fact, Salamon (1987) has argued that government provides substantial financial resources to the non-profit sector that in turn delivers the services, thereby replacing governmental provision. These are actually foundations of the so-called interdependence theory that claims the government is a partner to non-profits in the production of quasi-public goods, which means that complementary role of the non-profit sector and government exists in dealing with market and government failures.

Moreover, government – non-profit sector relationship has also been addressed in so-called social origins theory (Salamon and Anheier, 1998), which argues that the size of the non-profit sector is an outcome of power relations among different social classes and key social institutions. This indicates that no uniform relationship between the size of governmental social (welfare) spending and the size of the non-profit sector exists, since different non-profit regime types are proposed: statist, social-democratic, liberal and corporatist type (Salamon and Sokolowski, 2001).<sup>17</sup> In general, statist and social-democratic regimes are described by the fact that the socio-economic importance of the non-profit sector is relatively small (although in the latter regime due to the considerable amount of welfare services already provided by government; and in the former regime due to limitations on social activities imposed by the ruling elites in society), whereas in liberal and corporatist regimes the socio-economic importance of the non-profit sector is relatively large (although in the former regime

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<sup>17</sup> Kabalo (2009) has even suggested that there is a fifth non-profit regime, more related to power relations between social classes in decolonised and newly emerged states. She has argued that clashing patterns between welfare state and the size of the non-profit sector could be expected in those countries, depending mostly on the historical experience.

due to the relatively low governmental provision of welfare services, which are left for non-profit sector to be carried out; and in the latter due to the implication that the non-profit sector serves as traditional mechanism for extended governmental welfare policies provision).

In the context of supply side oriented approaches, the resource dependence approach describes the relations of the non-profit sector with government and business sectors as two important revenue sources of non-profit activity. This approach argues that resources available to the non-profit sector depend on the wealth of certain society (as a prerequisite for ability to contribute funds), as well as on the level of government spending (as currently the most important revenue source of non-profit organisations), which is in line with the assumptions of interdependence theory. Nevertheless, the resource dependence approach is also closely related to altruism and giving theories of the non-profit sector. These theories are very interdisciplinary in nature; they address psychological, sociological and economic aspects of individual philanthropy, altruism, charity and voluntarism (Mount, 1996). The perspective of these theories is focused on supply side, since they analyse those who supply the funds to support the work of non-profit organisations. Research findings suggest that giving is actually a »social exchange«; donors give funds to non-profit organisations in exchange for positive feelings, influence, and tax benefits (Kelly, 1998; Worth, 2009).<sup>18</sup> Regarding the latter, it should be acknowledged that often there are incentives to donate funds for (certain) purposes and activities of non-profit organisations in order to lower potential tax burden, predominantly in the form of tax deductions and tax credits. In fact, Mount (1996) has conducted a factor analysis based on survey data – the results of her analysis show that factors such as recognition, commemoration, and tax incentives help to explain approximately 18 per cent of variance in motivations for giving.<sup>19</sup>

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<sup>18</sup> It needs to be acknowledged that altruism and giving theories are micro oriented in their nature. This indicates that it is very difficult to verify them from cross-country perspective.

<sup>19</sup> Indeed, certain empirical research supports the idea that tax deductions and tax credits for donations to non-profit organisations increase the amount of donations, although it seems that donations are more related to the state of the economy (more on this see, e.g., De Vita and Twombly, 2004).

## 5. A brief overview of the existing empirical research

So far, several empirical studies have been performed trying to investigate the determinants of non-profit sector growth and development. However, there is lack of studies that are focused on the determinants of cross-country variations in the size of the non-profit sector. Namely, the existing studies are usually country specific, as for instance Corbin (1999) for metropolitan areas in the United States, Grønbjerg and Paarlberg (2001) for selected counties in the United States, or Luksetich (2008) for selected non-profit organisations in the United States etc.

Besides, the majority of studies investigate predominantly the reasons for the emergence and growth of the non-profit sector, or are they focused on verification of particular theories and their empirical effect on the size of the non-profit sector. For instance, positive relationship between income and availability of sources for non-profit sector has been suggested by several authors, both directly (e.g., Corbin, 1999) or indirectly (Grønbjerg and Paarlberg, 2001). The latter authors have also revealed that the size of the non-profit sector is more sensitive to opportunity structures created by community social and political conditions, meaning that supply side factors should be more important in determining the size of the non-profit sector.<sup>20</sup> Similarly, Luksetich (2008) has found out positive and statistically significant relationship between governmental grants and the number of the non-profit organisations in the United States.<sup>21</sup>

One of the few cross-country empirical researches has been performed by Salamon and Sokolowski (2001) for 24 selected countries. They have pointed out the positive relationship between governmental social spending and the amount of volunteer participation, although they have expected negative relationship due to the »crowding-out effect«. This means that they have actually supported the validity of interdependence theory and dismissed the validity of government failure theory. This research has been upgraded by Matsunaga, Yamauchi and Okuyama (2010), although they have argued more in favour of the government failure theory.

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<sup>20</sup> Ben-Ner and van Hoomissen (1992) have even suggested that wealth is an important determinant for the size of all sectors in the economy, and non-profit sector should be no exception.

<sup>21</sup> This notion has also been addressed to in other empirical studies. For instance, Bielefeld (2000) has also pointed out positive relationship between public social expenditures and size of the non-profit sector.

Nevertheless, there is a clear lack of cross-country oriented studies, potential factor being the lack of internationally comparable data. The approach taken in this study is to combine the experience of the existing studies and develop a cross-section econometric model, where the size of the non-profit sector, measured with the share of employment in the sector, tries to be explained with relevant economic, social, cultural and political factors. Consequently, the concepts and ideas of relevant non-profit theories are combined in development of econometric model. The main purpose of this research is to investigate the relationship between selected explanatory variables and size of the non-profit sector. The research would also like to determine, how much cross-country variation in the size of the non-profit sector could be explained with the selected explanatory variables. Following, data and methodology of research are presented.

## 6. Data and methodology

The purpose of the study is to identify and empirically verify the effect of potential factors, derived from the theories, hypotheses or concepts discussed above, on cross-country differences in the size of the non-profit sector. The empirical analysis is based on the sample of 38 countries, which is related to the fact that there is a limited amount of available and internationally comparable data on the size of the non-profit sector. The sample of analysed countries includes Argentina, Australia, Austria, Belgium, Brazil, Canada, Chile, Colombia, the Czech Republic, Denmark, Egypt, Finland, France, Germany, Hungary, India, Ireland, Israel, Italy, Japan, Kenya, Mexico, Morocco, the Netherlands, Norway, Pakistan, Peru, the Philippines, Poland, Portugal, Romania, Slovakia, South Africa, South Korea, Spain, Sweden, the United Kingdom and the United States. The main approaches evaluated in the study are demand and supply heterogeneity, resource dependence theory, interdependence theory and failure theories. However, it needs to be stressed once again that this is an exploratory study, which tries to provide insight into potential factors shaping the differences in the size of the sector among countries, and particularly, how much variation could be explained with those factors.<sup>22</sup>

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<sup>22</sup> Since many variables used in the analysis are not collected and reviewed on regular basis, the focus is more oriented towards the evaluation of the concepts discussed in the paper rather than on issues related to data quality.

The non-profit sector workforce as percent of the economically active population (TSWORKF) is used as a dependent variable, which is, according to Anheier (2000), one of the most commonly used measures for the size of the non-profit sector. As already noted, the data for this variable are derived from The John Hopkins Comparative Nonprofit Sector Project (2004) and refer to the collecting period of 1995–1999, except for Portugal, Canada, Chile and Denmark, where data refer to the years 2002, 2003 and 2004 respectively.

Among the explanatory variables, several economic, social, cultural and political variables are used in the analysis. The first explanatory variable describes supply-side heterogeneity of society, which could be measured with the level of income inequality in society. Therefore, Gini index (GINI) is used as a proxy for income inequality in society. Gini index measures the extent to which distribution of income between individuals and households in society deviates from a perfectly equal distribution. This means that larger values of the index indicate larger income inequality in society. The source of data for these measures is Human Development Report (2009) and relates to the period 1992–2007.

The second explanatory variable describes the level of democratic development of a society, which should try to explain the notion that socio-economic importance of the non-profit sector is the result of democratic development of society. Namely, the heterogeneity approach contemplates that the existence of the non-profit sector is the result of the development of democratic society and the capitalist economic system. In this context, it should be expected that the non-profit sector is larger in more democratic countries. The source of data for these measures is index of democracy (DEMOK) taken from Vanhanen (2000). This index tries to measure democracy with competition and participation, where the larger value of index denotes stronger democracy. The data relate to the year 2000, since they are taken from dataset version 2.0.

The third explanatory variable relates to resource dependence hypothesis, which contemplates that the development of the non-profit sector is related to the availability of resources to the sector. Variable real gross domestic product per capita in 1.000 purchasing power parity USD (GDPC) is used as a measure of wealth of a society, although it often does not reflect the wealth and development of society perfectly.<sup>23</sup> Source of data

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<sup>23</sup> Some non-mainstream economists claim that GDP levels imply some extent of statistical fallacy, since they do not take into account most of the real costs incurred to

for these measures is Freedom in the World Report (2002) and is related to the year 2000.

The fourth explanatory variable used in the analysis relates to interdependence and government failure hypotheses. This variable describes the size of government transfer expenditures in GDP (TRFEXP). It describes the amount of governmental welfare related spending; the study would like to portray whether this spending promotes or crowds out non-profit sector (social) activities. The data for this variable are taken from the Gwartney and Lawson (2009) dataset and relate to the year 2000. The existing data in the dataset have been modified for the purpose of the analysis. Initial ratings (originally denoted  $V_j$ ) for each country have been reversed by the formula  $10 - V_j$ . This modification should enable the countries with larger governmental transfer expenditure ratio to also have larger values of explanatory variable, so the relation between the size of government and the size of the non-profit sector could be directly tested.

Finally, in relation to demand side heterogeneity, three explanatory variables are used that describe ethnic (EF), linguistic (LF) and religious (RF) fragmentation of society. All three indexes are computed as one minus the Herfindahl index of ethnic, linguistic or religious group shares, where ethnic fragmentation considers not only linguistic, but also racial and physical characteristics, which are omitted if only linguistic fragmentation is taken into consideration.<sup>24</sup> The source of data for these measures is Alesina et al. (2003).

Table 2: Descriptive statistics

Variable	Mean	Standard Deviation
TSWORKF	4,7526	3,54925
GINI	36,6289	9,62454
DEMOK	26,3437	11,62630

produce goods and services, simply because these costs do not pass through markets and, consequently, do not get prices (e.g., costs of noise, air and water pollution etc.). This means that GDP levels need measure well-being in certain society adequately (see Mishan, 1993). Nevertheless, since the resource availability tends to depend on income, GDP per capita should reasonably be used to test this hypothesis.

<sup>24</sup> This distinction is particularly important for Latin American countries, which tend to be more homogeneous linguistically than ethnically. In contrast, linguistic fragmentation has larger tendency to also reflect ethnic fragmentation in European countries. More on the reasons for separation of the two measurements of fragmentation see Alesina et al. (2003). Still, some extent of correlation between these two measures should be expected.

GDPC	15,4825	9,24677
TRFEXP	3,9574	2,21297
EF	0,3006	0,2407
LF	0,2791	0,27203
RF	0,4137	0,23561

Descriptive statistics is presented in Table 2. The mean share of non-profit sector workforce in economically active population for selected 38 countries is approximately 4.75%; maximum value is found in the Netherlands (14.4%) and minimum value in Mexico (0.4%). The mean value of Gini index is approximately 36; minimum value is found in Denmark at 24.7 and maximum value in Colombia at 58.5 (largest income inequality in the sample). The mean value of Vanhanen's index of democracy is approximately 26, minimum value is found in Pakistan and maximum value in Italy, whereas the mean value of GDP per capita in the sample is approximately 15.500 PPP USD, minimum value is found in Kenya, just slightly above 1.000 USD and maximum value in the United States, almost 32.000 USD. The mean value of the governmental transfer expenditure variable is approximately 3.96, minimum value of variable is found in Pakistan and maximum value is found in France with the largest extent of governmental transfer expenditure (in GDP) in the sample. The mean value of the ethnic fragmentation of society is 0.30, minimum value is found in South Korea at 0.002 and maximum value in Kenya at 0.86 as the most ethnically fragmented society in the sample. Regarding the last two explanatory variables, the mean value of linguistic fragmentation is approximately 0.28; minimum and maximum values are also found in South Korea and Kenya (although in this case at almost 0.89). The mean value for religious fragmentation is approximately 0.41; minimum value is found in Morocco at 0.0035 and maximum value in South Africa at 0.86 as the most religiously fragmented society in the sample.

## 7. Findings

The results of the empirical analysis, that is correlation and multiple regression analysis, provide support for most of the explanatory variables used in the model. Bivariate Pearson correlation coefficients are presented in Table 3. These correlation coefficients show whether two variables have a perfect linear relationship (value 1) or there is absence of one (value 0).

The strongest relationship is between gross domestic product per capita and the share of non-profit sector workforce in economically active population ( $r = 0.79$ ;  $p < 0.01$ ). The relationship between democracy and the third sector workforce is also positive and statistically significant ( $r = 0.48$ ;  $p < 0.01$ ). This in a way supports the idea that the third sector is the result of democratic development of society. The relationship between governmental transfer spending and non-profit sector workforce is also positive and statistically significant, which supports the idea that the non-profit sector supplements government in social and welfare policy implementation. Notwithstanding, the relationship between Gini index and non-profit sector workforce is negative, although rather weak and also statistically insignificant. Nevertheless, the sign of coefficient is in line with the idea that social cohesion is associated with larger non-profit sector. The same goes with the relationship between non-profit sector workforce and linguistic/religious fragmentation of society. The relationship is positive in both instances, which is in line with the idea of culturally fragmented societies having a larger non-profit sector, although both relationships are rather weak and statistically insignificant. Finally, the relationship between ethnic fragmentation and non-profit sector workforce is negative. This is not in line with theoretical predictions, although this relationship is also statistically insignificant.

Table 3: Zero-order correlations of variables included in the model<sup>25</sup>

	TSWORKF	GINI	DEMOK	GDPC	TRFEXP	EF	LF	RF
TSWORKF	1	-,240	,482**	,786**	,480**	-,182	,010	,217
GINI	-,240	1	-,471**	-,513**	-,551**	,578**	,217	-,005
DEMOK	,482**	-,471**	1	,728**	,818**	-,571**	-,307*	,094
GDPC	,786**	-,513**	,728**	1	,641**	-,474**	-,321*	,223
TRFEXP	,480**	-,551**	,818**	,641**	1	-,494**	-,335*	,020
EF	-,182	,578**	-,571**	-,474**	-,494**	1	,631**	,149
LF	,010	,217	-,307*	-,321*	-,335*	,631**	1	,277*
RF	,217	-,005	,094	,223	,020	,149	,277*	1

<sup>25</sup> \*\* means  $p < 0,01$ ; \* means  $p < 0,05$ ; one-tailed test.

The results of the ordinary least squares regression analysis (OLS) are presented in Table 4. Multiple regression measures the effect each explanatory variable has on the dependent variable while controlling for the effects of all other selected (included) variables. Explanatory variables are listed in the left-hand column, whereas non-standardised and standardised coefficients, standard errors and statistical significance of the coefficients are presented in other columns.

Table 4: Multiple regression analysis

Explanatory variables		Dependent variable TSWORKF				
		Coefficient	Standard Error	Beta	t-value	Significance
1	Constant	-5,372	2,111	/	-2,545	,016
	GINI	,119	,047	,322	2,538	,017
	DEMOK	-,123	,057	-,402	-2,136	,041
	GDPC	,423	,054	1,102	7,779	,000
	TRFEXP	,552	,268	,344	2,061	,048
	EF	-2,137	2,261	-,145	-,945	,352
	LF	5,232	1,637	,401	3,197	,003
	RF	-1,292	1,473	-,086	-,877	,387
	N	38		SEE	1,8847	
	R <sup>2</sup> <sub>ADJ</sub>	0,718		F (Sig.)	14,460 (0,000)	

The results provide support for the majority of explanatory variables included in the model, except for the variables describing ethnic and religious fragmentation, where regression coefficients are not statistically significant. This may be due to a potential problem associated with multicollinearity, since relatively high pair-wise correlation between variables describing ethnic and linguistic fragmentation can be observed (although this correlation is not excessively high). Since the main goal of the analysis is providing an assessment how well the model predicts cross-country variations in the size of the non-profit sector, the issue of multicollinearity should not be seen as a problem that needs to be addressed further, especially if we want to avoid creating specification bias of the model.<sup>26</sup>

Nevertheless, the adjusted R<sup>2</sup> value even suggests that the selected seven explanatory variables explain almost three quarters of variation in the size

<sup>26</sup> More on this issue see Gujarati (2003) and Motulsky (2010).

of the non-profit sector among 38 analysed countries. Particularly notable is the effect of the variable gross domestic product per capita, which is the most important explanatory variable in the model. This indicates that supply-side factors, such as the availability of the sources to the sector, seem to be more important in explaining cross-country differences in the size of the non-profit sector. Consequently, the notion that socio-economic importance of the sector is related to economic development of a society is also strengthened. Besides, the effect of the variable describing linguistic fragmentation of society, a measure of demand heterogeneity, supports the idea that diversity in society positively contributes to the size of the non-profit sector, which obviously represents a place where different needs of various (cultural) groups in pluralistic societies are met. Similarly, the effect of socio-economic heterogeneity of society and the effect of the level of democracy in society are also statistically significant. Finally, the positive and statistically significant effect of the government transfer expenditure should also be stressed, as it indicates that non-profit sector basically complements welfare state programmes.<sup>27</sup>

## 7. Concluding reflections

Findings presented in the study are generally consistent with most of the theoretical concepts discussed. Interestingly, seven explanatory variables used in the multiple regression model explain almost three quarters of variation in the size of the non-profit sector among 38 countries in the sample. This should not be neglected, especially if we take into that cross-sectional data are used. In particular, gross domestic product per capita has the largest explanatory power in the model, suggesting that resource availability, derived from the wealth of society, is the most significant factor in explaining cross-country variations in the size of the non-profit sector. This compares favourably to the findings of Ben-Ner and van Hoomissen (1992) or Corbin (1999), and specifically tends to promote the role of wealth in sector development. Similarly, the positive effect of government transfer expenditure on the variations in the size of the non-profit sector is also noteworthy, which is in line with findings of Bielefeld (2000) or Salamon and Sokolowski (2001) and tends to imply some sort of

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<sup>27</sup> Still, the existence of various non-profit sector regimes derived from social origins theory should be rejected per se.

partnership or interdependence between government and the non-profit sector, although this does not reject per se the validity of the social origins theory and its aforementioned four (five) non-profit regime types. Namely, countries can be placed into different regime types given the specific relations between the size of social (transfer) spending and size of the non-profit sector, but statistical relationship between those two variables seems to be positive. Moreover, the results should be interpreted bearing in mind the purpose of the paper, which is associated with explaining overall cross-country variance in the size of the non-profit sector.

Nonetheless, demand side heterogeneity, in particular linguistic fragmentation of society, has also positive effect on the size of the non-profit sector, which is in line with Weisbrod's (1998) predictions. Other two measures of demand heterogeneity are not statistically significant and they even have extremely large standard errors, perhaps due to the multicollinearity, so the evidence on their effect is rather inconclusive. In this context, the real problem of the analysis is the lack of internationally comparable data on the size of the non-profit sector, both from cross-country and from time frame perspectives, which prevents the analysis to be performed on a larger sample. This would enable more accurate estimates and even provide a tool for possible elimination of multicollinearity problem. Nevertheless, since this study is more exploratory in nature, it should be seen as a basis for additional research on the macro and micro factors causing cross-country variations in the size of the non-profit sector.

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## RAZLIKE U VAŽNOSTI NEPROFITNOG SEKTORA U RAZLIČITIM ZEMLJAMA

### Sažetak

Neprofitni je sektor vrlo raznolik i sastoji se od organizacija koje služe nekom zajedničkom cilju. Aktivnosti toga sektora primarno se temelje na idejama individualizma i zajedništva, što je i određena vrsta tehničke različitosti od vladinog odnosno javnog sektora. Neprofitni se sektor pojavio zbog nekoliko potencijalnih razloga, no kao najvažniji razlozi u literaturi se navode neuspjeh i tržišta i države da građanima pruže određene proizvode i usluge, zatim pojava zajedništva i osobne slobode u modernim društvima te povećana potreba za solidarnošću među ljudima. U osnovi, razvoj neprofitnog sektora posljedica je razvoja demokracije i kapitalizma. Podaci upućuju na značajan porast društveno-ekonomske važnosti neprofitnog sektora zadnjih desetljeća. Međutim, postoje značajne razlike u veličini neprofitnog sektora među zemljama. Stoga se rad bavi empirijskim istraživanjem potencijalnih čimbenika koji utječu na te razlike. Glavni pristupi koje se istražuje u empirijskoj studiji su razlika ponude i potražnje, teorija ovisnosti o sredstvima, teorija međuovisnosti i teorije neuspjeha. Eksplanatorne varijable korištene pri analizi višestruke regresije objašnjavaju gotovo tri četvrtine razlika u veličini neprofitnog sektora među 38 zemalja iz uzorka. Bruto domaći proizvod po glavi stanovnika ima najveću vrijednost za objašnjenje u modelu, sugerirajući da je raspoloživost sredstava, koja se izvodi iz bogatstva pojedinog društva, najvažniji čimbenik za objašnjavanje razlika u veličini neprofitnog sektora među zemljama. Očito je da su čimbenici koji djeluju na strani ponude važniji za objašnjavanje veličine sektora u pojedinim zemljama od onih koji djeluju na strani potražnje.

Ključne riječi: neprofitni sektor, veličina neprofitnog sektora, koncepti neprofitnog sektora, čimbenici na strani ponude i na strani potražnje, empirijska analiza