

# **FINANCIAL PRACTICES AND PROGRAM EFFICIENCY OF NON-GOVERMENTAL ORGANIZATIONS IN NAIROBI CITY COUNTY, KENYA**

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## **ABSTRACT**

The increasing demand for accountability and efficient utilization of donor funds has intensified pressure on non-governmental organizations (NGOs) to enhance program performance. In Kenya, particularly in Nairobi City County, NGOs continue to face challenges related to financial management practices, which undermine program efficiency in resource-constrained and donor-dependent environments. Program inefficiencies have been linked to weak financial systems, poor resource allocation, and limited organizational capacity. While external funding uncertainties persist, financial practices remain a critical internal mechanism that NGOs can leverage to improve program outcomes. This study aimed to investigate

the effect of financial practices on program efficiency among NGOs operating in Nairobi, Kenya. The specific objectives were to examine the effects of liquidity management, budgeting practices, financial reporting quality, and financial sustainability on program efficiency, as well as to assess the mediating role of resource allocation efficiency and the moderating role of organizational capacity in this relationship. The study was anchored on Agency Theory, Pecking Order Theory, and Financial Accountability Theory.

**Key words:** Financial practices, Program efficiency, Liquidity management, Budgeting practices, Financial reporting, Financial sustainability.

## **INTRODUCTION**

### **Background of the study**

Non-governmental organizations (NGOs) play a pivotal role in socio-economic development by providing humanitarian assistance, health services, education, environmental conservation, and poverty alleviation programs, particularly in developing countries. In Kenya, and notably within Nairobi City County, NGOs remain instrumental in bridging development gaps that government and private sector actors cannot fully address. Despite their growing relevance, NGOs face heightened scrutiny from donors, regulators, and beneficiaries concerning financial accountability, resource utilization, and program effectiveness (World Bank, 2021).

Organizational performance in the non-profit sector is often analyzed from two perspectives. The first emphasizes internal organizational factors, including financial management practices, governance structures, resource allocation, and managerial competencies, as key determinants of efficiency and effectiveness (Anthony & Young, 2023). The second perspective focuses on external factors, such as donor requirements, regulatory frameworks, funding volatility, and macroeconomic conditions, which shape NGO operations (OECD, 2020). Contemporary

research highlights an integrated approach, recognizing that NGO performance arises from the interaction between internal financial capabilities and external regulatory and funding environments (Ebrahim, Battilana, & Mair, 2022).

Financial practices have emerged as a critical internal mechanism influencing program efficiency. Liquidity analysis, through metrics like the current ratio, quick ratio, and cash flow adequacy, provides insights into an NGO's capacity to meet short-term obligations and sustain activities without disruption (Keating, Fischer, Gordon, & Greenlee, 2021). Inadequate liquidity has been linked to project delays and inefficient resource utilization, particularly in donor-dependent NGOs (Cordery & Sim, 2022). Budgeting practices guide financial planning, expenditure control, and alignment with strategic objectives. Effective budgeting, measured through variance analysis and consistency between budgets and program plans, improves cost control and ensures resources target priority activities (Horngren, Datar, & Rajan, 2021). Empirical evidence suggests that NGOs with robust budgeting systems achieve higher program targets and improved cost-benefit outcomes (Muriithi & Waweru, 2023).

Financial reporting quality also significantly affects NGO performance. Timely, accurate, and compliant reports strengthen transparency, foster donor confidence, and enable informed managerial decisions (International Federation of Accountants [IFAC], 2022). Weak reporting has been associated with inefficiencies, delayed funding, and resource misallocation (OECD, 2021). Financial sustainability, the capacity to maintain operations over time, is another determinant of NGO performance. Indicators include funding diversity, adequate reserves, and reduced donor dependency (Bowman, 2022). NGOs in Nairobi face unique sustainability challenges due to donor fatigue, shifting priorities, and competition for limited resources (NGO Coordination Board, 2023). Organizations with narrow funding bases are especially vulnerable to program disruptions, affecting efficiency and long-term impact.

While financial practices directly influence program efficiency, resource allocation efficiency—the timeliness and appropriateness of fund distribution—serves as a critical mediating factor. Even well-designed budgets and sound financial systems may fail to yield efficient programs if resources are not disbursed promptly (Ebrahim et al., 2022). Delays in fund release negatively impact project timelines, resource utilization, and target achievement (World Bank, 2022). Given this context, understanding how financial practices influence program efficiency through resource allocation efficiency is vital for improving NGO effectiveness in Nairobi City County. This study seeks to provide empirical evidence to inform financial management, donor policies, and regulatory oversight in Kenya's non-profit sector.

### **Program Efficiency**

Program efficiency refers to the extent to which an organization delivers programs and services using minimal resources while achieving intended outcomes. For NGOs, program efficiency is crucial due to resource constraints, donor accountability pressures, and high expectations for social impact (Ebrahim & Rangan, 2024). Efficient programs ensure financial, human, and material resources generate meaningful outputs and outcomes for target populations. Scholars conceptualize program efficiency as the relationship between inputs, processes, and outputs,

emphasizing value for money and optimal resource utilization (OECD, 2021). Key indicators include cost–benefit ratio, timeliness of implementation, resource utilization rates, and achievement of program targets. A favorable cost–benefit ratio reflects higher social value relative to expenditure, while timely implementation indicates effective planning and coordination (World Bank, 2022).

Timeliness is critical, as delays increase costs, reduce donor confidence, and decrease the relevance of interventions (Cordery & Sim, 2022). Resource utilization measures how effectively funds, personnel, and assets support program activities without waste. High utilization rates correlate with strong managerial control and efficient operations (Keating et al., 2021). Achievement of program targets captures the effectiveness dimension of program efficiency, linking operations to intended social outcomes. NGOs consistently meeting targets demonstrate alignment between planning, financing, and execution (Ebrahim & Rangan, 2024). Studies show program efficiency is influenced by sound financial practices, timely resource disbursement, and effective monitoring mechanisms (Muriithi & Waweru, 2023). In Nairobi, where NGOs face intense donor competition and regulatory oversight, program efficiency is a key determinant of organizational sustainability and credibility. Understanding the drivers of program efficiency is therefore essential for enhancing performance and development impact.

### **Financial Practices**

Financial practices encompass the policies, procedures, and activities an organization employs to plan, manage, control, and report financial resources. In NGOs, financial practices are critical due to reliance on donor funds and limited internal revenue (Anthony & Young, 2023). Effective financial practices enhance accountability and program efficiency. For liquidity analysis, measures like current ratio, quick ratio, and cash flow adequacy indicate an NGO’s ability to meet short-term obligations are used. Adequate liquidity ensures uninterrupted operations, while weak liquidity delays project implementation and leads to inefficient resource use (Keating et al., 2021; Mutua, 2023). For budgeting, sound budgeting ensures resources align with program priorities and minimizes wastage are considered. Budget variance analysis, accuracy, and plan alignment support cost control, forecasting, and timely program execution (Wanjuki, 2023; Kazanskaia, 2025). For financial reporting, timely, accurate, and compliant reports enhance transparency and donor confidence are used. High-quality reporting supports informed decision-making and reduces misallocation risks (Omondi, 2021; Omaru et al., 2025). For financial sustainability, indicators include funding diversity, reserves, and reduced donor dependency, ensuring operational continuity and resilience to funding shocks (Dadu, 2024; Oluoch et al., 2021).

### **Organizational Capacity**

Organizational capacity is the ability to mobilize, manage, and coordinate human, financial, technical, and structural resources to achieve strategic objectives. In NGOs, it determines how financial inputs and allocations translate into sustainable program outcomes (Ebrahim & Rangan, 2024; Keating et al., 2021). Skilled and sufficient staff improve budgeting, reporting, and monitoring effectiveness. NGOs with competent personnel better manage funds and

achieve program targets (Muriithi, Cordery & Sim, 2022). Effective boards and management teams provide direction, enforce financial discipline, and align programs with organizational mission (Anthony & Young, 2023; Omondi, 2021). Robust financial management systems, monitoring frameworks, and internal controls facilitate timely resource disbursement and accurate expenditure tracking (Keating et al., 2021; Naisiae & Mungai, 2024). Organizational capacity moderates the relationship between financial practices and program efficiency, determining whether sound financial systems yield effective outcomes. It is operationalized using the staff-to-workload ratio.

### **Resource Allocation Efficiency**

Resource allocation efficiency measures how effectively an organization distributes financial and non-financial resources to programs in a timely, coordinated, and need-based manner (Abdi Hussein Golicha et al., 2022). Timeliness of disbursement reflects speed of fund release to implementing units. Delays compromise schedules, inflate costs, and reduce efficiency (Naisiae & Mungai, 2024). The indicator used herein, resource allocation efficiency, mediates the relationship between financial practices and program efficiency, ensuring that liquidity, budgeting, reporting, and sustainability translate into effective program outcomes (CALP Network, 2020; Naisiae & Mungai, 2024).

### **Non-Governmental Organizations (NGOs) in Kenya**

NGOs in Kenya operate under the Public Benefits Organizations (PBO) Act, 2013, and are overseen by the Public Benefits Organizations Regulatory Authority (PBORA). As of 2024, over 14,000 NGOs operate across sectors including humanitarian relief, health, education, environmental conservation, governance, poverty alleviation, and community development (PBORA, 2024). The sector has expanded due to social needs, donor funding, and partnerships with government and private actors. Competition among local and international NGOs, including World Vision, CARE International, Oxfam, Save the Children, and Action Against Hunger, requires innovative operational models and strategic approaches (Wanyama, 2022). Technological advancements, such as digital platforms for program delivery, monitoring, and fundraising, have enhanced NGO efficiency and accountability (Karanja & Otieno, 2023; Mutua & Wambua, 2021). However, challenges remain, including cybersecurity risks, delayed funding, and rising operational costs (Cardoso et al., 2025; PBORA, 2024). Nairobi City County serves as a hub for NGO headquarters, international agencies, donor offices, and regulatory institutions, making it a suitable context to examine organizational mechanisms, financial practices, and program efficiency.

### **Statement of the Problem**

NGOs in Kenya play a vital role in addressing social and economic challenges, yet their effectiveness depends on sound financial practices such as liquidity management, budgeting, reporting, and sustainability (Kimonge, 2011). Weak financial practices impede program efficiency, affecting cost-benefit ratios, timely implementation, resource utilization, and target achievement (Mutua, 2023).

Evidence from the U.S., Nigeria, and Kenya demonstrates the critical role of financial practices in improving NGO performance (Niswonger, 2023; Daberechi, 2021; Omondi, 2021).

However, limited research integrates multiple financial practices to examine their collective effect on program efficiency, especially in Nairobi-based NGOs. This study seeks to fill these gaps by providing localized evidence to inform managerial decision-making and optimize resources.

## **Objectives of the Study**

### **General Objective**

To investigate the effect of financial practices on the program efficiency of NGOs in Nairobi, Kenya.

### **Specific Objectives**

- i. To determine the effect of liquidity management on program efficiency.
- ii. To establish the effect of budgeting practices on program efficiency.
- iii. To establish the effect of financial reporting quality on program efficiency.
- iv. To determine the effect of financial sustainability on program efficiency.
- v. To establish the mediating role of resource allocation efficiency in the relationship between financial practices and program efficiency.
- vi. To determine the moderating role of organizational capacity on the relationship between financial practices and program efficiency.

### **Research Hypotheses**

**H01:** Liquidity management has no significant effect on program efficiency.

**H02:** Budgeting practices have no significant effect on program efficiency.

**H03:** Financial reporting quality has no significant effect on program efficiency.

**H04:** Financial sustainability has no significant effect on program efficiency.

**H05:** Resource allocation efficiency does not significantly mediate the relationship between financial practices and program efficiency.

**H06:** Organizational capacity does not significantly moderate the relationship between financial practices and program efficiency.

### **Significance of the Study**

The study provides practical and academic value by guiding NGO management to optimize financial practices, improve program delivery, and enhance organizational effectiveness. It will also help in developing diagnostic frameworks and models linking financial practices, resource allocation, and program efficiency. Finally, it will offer empirical evidence for Nairobi-based NGOs to adopt evidence-based financial strategies for sustainability and operational efficiency.

### **Scope of the Study**

The study focuses on NGOs operating in Nairobi City County between 2020 and 2024. Independent variables include financial practices, while dependent variables are program efficiency and financial performance. Resource allocation efficiency serves as a mediating variable, and organizational capacity as a moderating variable. The study is guided by Agency Theory, Pecking Order Theory, and Financial Accountability Theory.

## **LITERATURE REVIEW**

### **Introduction**

This chapter presents a review of literature relevant to the study on financial practices and program efficiency among NGOs in Nairobi City County. It examines theoretical perspectives guiding financial management and empirical studies related to the study variables. The chapter critically evaluates prior research to highlight existing knowledge gaps and discusses the mediating role of resource allocation efficiency in linking financial practices to program outcomes. Finally, it presents a conceptual framework demonstrating the relationships among the key variables of the study.

### **Theoretical Review**

The study is anchored on three finance-related theories: Agency Theory, Pecking Order Theory, and Financial Accountability Theory.

#### **Agency Theory**

Agency Theory, conceptualized by Jensen and Meckling (1976), suggests that conflicts may arise when principals, such as donors, delegate control of resources to agents, such as NGO managers. Informational asymmetry between principals and agents creates opportunities for moral hazard and adverse selection. Managers may pursue personal objectives rather than organizational goals, potentially reducing program efficiency.

In NGOs, Agency Theory provides insight into risk management and financial sustainability.

Robust mechanisms such as internal controls, audits, and financial reporting align managers' actions with donor expectations (Eisenhardt, 1989). Empirical evidence in Kenya supports this framework. Mbiti (2017) found that high agency costs due to weak monitoring correlated with lower operational efficiency. Similarly, Mwangi (2014) reported that rigorous financial accountability positively influenced NGO efficiency in Nairobi. Chelangat (2018) highlighted that planning, monitoring, and controls enhance financial sustainability, while Kamunya and Chege (2025) showed that structured risk management improves project outcomes. Therefore, Agency Theory helps explain how managerial behavior and financial practices jointly influence program efficiency.

#### **Pecking Order Theory**

Pecking Order Theory, introduced by Donaldson (1961) and formalized by Myers and Majluf (1984), argues that organizations prefer internal funds first, debt second, and equity as a last resort due to asymmetric information. Internal resources are less costly, while external financing may signal financial risk.

In NGOs, this theory explains funding choices. Calabrese (2011) suggests that nonprofits prioritize unrestricted internal revenues before resorting to external funding. Fritz (2015) emphasizes that managers use debt cautiously to retain internal reserves. Pecking Order Theory thus provides a framework for understanding financial sequencing and resource allocation in NGOs, which directly influences operational flexibility, sustainability, and program efficiency.

### **Financial Accountability Theory**

Financial Accountability Theory focuses on reporting, justification, and management of financial decisions to stakeholders. In NGOs, accountability entails transparent planning, monitoring, control, and reporting of funds. Studies in Nairobi, such as Chelangat (2018) and Mwangi (2014), demonstrate that financial accountability improves sustainability and operational performance. Kabene (2021) highlights that competence in planning, reporting, and financial management enhances donor trust. Nurdiani et al. (2025) emphasize transparency and accountability as central to nonprofit legitimacy. Financial Accountability Theory underpins the assumption that robust financial systems foster stakeholder trust and enable efficient program implementation.

### **Empirical Review**

This section reviews past studies on financial practices, including liquidity analysis, budgeting, financial reporting, and financial sustainability, and their effect on program efficiency. It also explores resource allocation efficiency as a mediating variable linking financial practices to program outcomes.

### **Liquidity Analysis and Program Efficiency**

Niswonger (2023) found that insufficient liquidity constrains program delivery in US nonprofits, whereas effective liquidity management improves implementation efficiency. Rotinsulu and Nurnajamuddin (2021) observed that budget engagement, transparency, and internal control positively affect financial performance in Indonesia, with implications for accountability. Feng (2024) highlighted that global nonprofits with strong liquidity and governance maintain operational efficiency. Locally, Kimonge (2011) and Mutua (2023) confirmed that effective cash flow management and liquidity planning in Kenyan NGOs support program achievement. Khoza et al. (2025) demonstrated that high liquidity reduces risk and improves overall performance, reinforcing the importance of liquidity for program efficiency in Nairobi NGOs.

### **Budgeting and Program Efficiency**

Kazanskaia (2025) highlighted that structured budgeting and participative planning improve resource allocation in global nonprofits. Daberechi (2021) and Esuku (2022) found that detailed budget planning and monitoring positively affect performance in African NGOs and SMEs. In Nairobi, Wanjuki (2023) demonstrated that participative budgeting and forecasting enhance NGO performance. Wangai and Mungai (2019) showed that proper accounting and financial management improve loan and operational performance, indirectly highlighting the role of budgeting in NGO efficiency. Kativa (2013) and Kimani (2014) provided further evidence that budget participation and control strengthen program delivery.

### **Financial Reporting and Program Efficiency**

Gofe, Kebede, and Jiru (2021) found that timely financial reporting enhances accountability and program efficiency in Ethiopian NGOs. Omondi (2021) reported that strong governance improves report quality and program outcomes in Nairobi NGOs. Omaru et al. (2025) and

Mwaura (2013) confirmed that accurate, transparent, and timely financial reporting builds donor trust and supports efficient program delivery. Mugenyi et al. (2020) showed that integrated financial systems (IFMIS) enhance reporting accuracy, while Muli and Musau (2024) emphasized that internal controls improve reporting and operational performance.

### **Financial Sustainability and Program Efficiency**

Sontag-Padilla et al. (2019) noted that diversified revenue and long-term planning sustain programs globally. Dadu (2024) highlighted that NGOs dependent on donor grants struggle without strategic financial planning. Mutua (2023) found that financial sustainability supports continuous program delivery in Nairobi NGOs. Oluoch et al. (2021) and Alice et al. (2025) showed that strong internal controls and strategic planning enhance sustainability and program efficiency. Complementary studies in Kenyan banking (Adhing'a & Gatauwa, 2023; Malalu & Njoka, 2024; Ouma & Ndede, 2020) illustrate the role of financial risk management and technology adoption in operational efficiency, reinforcing applicability to NGO financial practices.

### **Organizational Capacity, Financial Practices, and Program Efficiency**

Light (2004) emphasized that leadership, governance, and skilled personnel enhance organizational capacity, enabling effective application of financial practices. Kazanskaia (2025) and Wairia & Nyangaria (2025) reported that governance reforms, HR development, and adaptive systems improve program outcomes. Okeyo (2023) confirmed that strong internal capacity converts financial insights into effective program results, highlighting its moderating effect on the relationship between financial practices and program efficiency.

### **Resource Allocation Efficiency, Financial Practices, and Program Efficiency**

Abdi Hussein Golicha et al. (2022) found that NGOs with efficient cash-transfer systems achieved timely fund disbursement and better program performance. Naisiae and Mungai (2024) reported that advanced M&E tools improve resource tracking, aligning disbursement with milestones. The CALP Network (2020) highlighted that delayed cash transfers reduce program efficiency globally. These findings support the conceptualization of resource allocation efficiency as a mediating variable between financial practices and program outcomes.

### **Conceptual Framework**

Smyth (2004) posits that a clearly structured conceptual framework aids in illustrating the potential relationships among the study variables. The conceptual framework for this research is presented graphically in Figure 1.

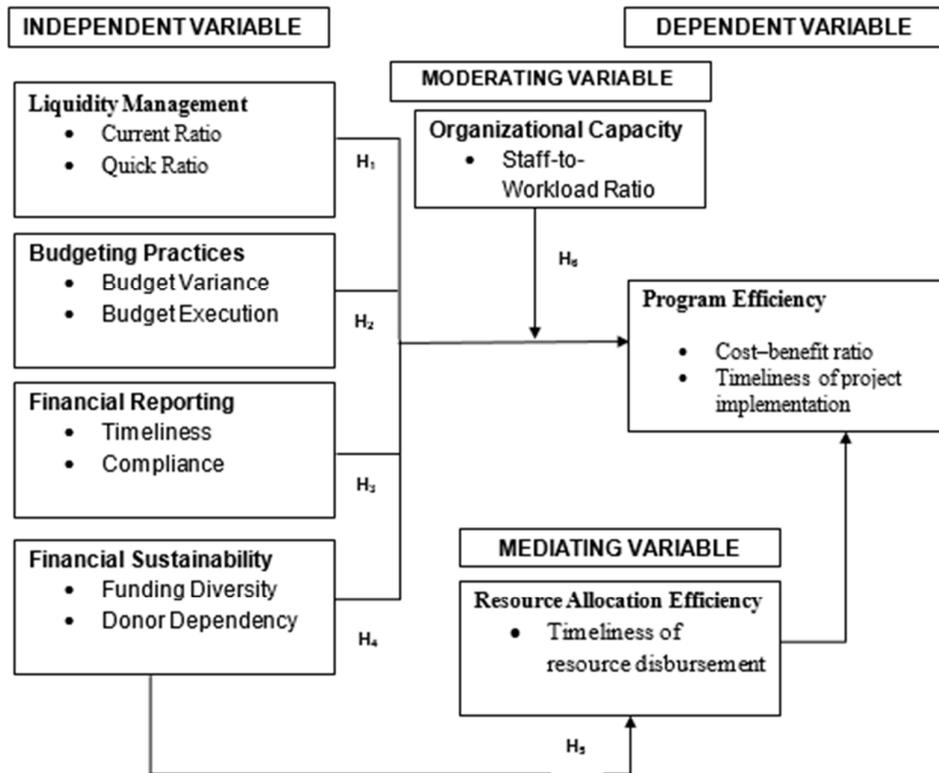


Figure 1: Conceptual Framework

Source: Author (2026)

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