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DONOR FUNDING FLEXIBILITY AND FINANCIAL PERFORMANCE OF NON-GOVERNMENTAL ORGANIZATIONS IN NAIROBI, KENYA

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ABSTRACT

Purpose of the Study: This study examined the effect of donor funding flexibility on the financial performance of Non-Governmental Organizations (NGOs) in Nairobi, Kenya.

Problem Statement: Although donor funding remains the primary source of financing for many NGOs, funding conditions may influence how resources are allocated and utilized. Limited empirical evidence exists on the effect of donor funding flexibility on the financial performance of NGOs, particularly in terms of funds utilization efficiency among NGOs in Nairobi.

Methodology: The study adopted a descriptive research design targeting NGOs registered with the Non-Governmental Organizations Co-ordination Board and operating in Nairobi. Primary data was collected from executive managers, finance managers, accountants, and program managers using structured questionnaires, while secondary data was obtained from NGO Board reports. Data was analyzed using descriptive statistics, Pearson correlation, and simple linear regression analysis.

Results of the Study: The findings revealed a positive and significant relationship between donor funding flexibility and financial performance ($r = 0.740$, $p < 0.01$). Regression results further established that funding flexibility has a positive and statistically significant effect on financial performance ($\beta = 0.483$, $p < 0.001$). The results indicate that NGOs operating under flexible donor funding arrangements are more likely to allocate resources efficiently, respond to changing operational needs, and achieve higher levels of funds utilization efficiency.

Conclusion and Policy Recommendation: The study concludes that donor funding flexibility is an important determinant of financial performance among NGOs. The study recommends that donor agencies adopt more flexible funding arrangements that provide NGOs with greater discretion in resource allocation while maintaining appropriate accountability mechanisms. NGOs should also strengthen internal financial management systems to ensure effective utilization of donor resources.

Keywords: *Donor, Funding Flexibility, Financial, Performance, Non-Governmental, Organizations*

INTRODUCTION

Non-Governmental Organizations (NGOs) play an important role in global development by complementing government efforts in the delivery of social services, humanitarian assistance, environmental conservation, and community development initiatives. Their growing involvement in addressing social and development challenges has made them important actors in global value creation and governance (Teegen, Doh, & Vachani, 2004). However, the ability of NGOs to fulfil their mandates depends significantly on the availability and effective allocation of financial resources, with many NGOs relying on funding from external donors (Werker & Ahmed, 2008).

In Africa, including Kenya, donor funding is a major source of financial support for NGOs. Through grants and development assistance, donors provide resources that enable organizations to implement programs and deliver essential services. However, donor funding is often accompanied by conditions relating to expenditure, reporting, accountability, and program implementation. While such requirements promote transparency and responsible stewardship of resources, they may also influence financial decision-making and resource allocation (Banks, Hulme, & Edwards, 2015). Consequently, donor-NGO relationships have important implications for organizational autonomy, planning, and resource management (Najam, 1996).

Funding flexibility refers to the extent to which donor resources are provided with limited restrictions, allowing recipient organizations greater discretion in allocating and utilizing funds according to operational priorities and emerging needs (UNHCR, 2024). Flexible funding enables NGOs to adjust resource allocations and respond to changing circumstances, whereas restrictive conditions may limit resource management decisions. Donor requirements can therefore influence NGO operations, priorities, and resource utilization (Wallace, Bornstein, & Chapman, 2006). At the same time, NGOs are expected to maintain transparency and accountability in the use of donor resources (Ortega-Rodríguez, Licerán-Gutiérrez, & Moreno-Albarracín, 2020). These considerations underscore the need to balance funding flexibility with accountability to ensure effective utilization of financial resources.

Growing emphasis on donor accountability has increased attention to how NGOs manage and utilize financial resources. As a result, funds utilization efficiency has emerged as an important indicator of financial performance. Efficient utilization of funds enhances accountability, minimizes wastage, and improves program effectiveness (Teegen et al., 2004). It also strengthens organizational effectiveness and donor confidence (Miriti & Karithi, 2020). Globally, development and humanitarian organizations increasingly recognize the value of flexible funding in responding to changing needs and operational priorities. Flexible funding provides organizations with greater discretion to allocate resources where they are most needed and respond to emerging challenges (UNHCR, 2024). Similarly, Smillie (2001) emphasizes the importance of supportive donor relationships in strengthening local organizational capacity and responsiveness.

In Kenya, particularly in Nairobi, NGOs operate in a highly competitive donor environment characterized by changing donor priorities, increasing accountability requirements, and growing demands for measurable impact. Restrictive funding conditions, delayed approvals, and resource allocation limitations may constrain efficient resource utilization and organizational performance (Miriti & Karithi, 2020). Delays in donor disbursements have also been associated with operational inefficiencies and implementation challenges among NGOs (Mureithi, 2019). Despite growing recognition of funding flexibility within development practice, existing studies have largely focused on organizational sustainability, donor dependency, and financial performance in general (Smillie, 2001). This paper therefore evaluates the effect of funding flexibility on funds utilization efficiency among NGOs in Nairobi, Kenya.

STATEMENT OF THE PROBLEM

NGOs have become important development partners in addressing social, economic, humanitarian, and environmental challenges, particularly where public-sector capacity is limited (Teegen, Doh, & Vachani, 2004). However, their ability to achieve intended outcomes depends partly on the effective utilization of donor resources. Despite substantial donor support, NGOs continue to face challenges related to resource allocation, program implementation, and the effective use of available funds (Mureithi, 2019). Growing demands for accountability, transparency, and measurable results have further increased the need for efficient resource utilization and sound financial management (Miriti & Karithi, 2020). Funding flexibility has emerged as an important factor that may influence how NGOs manage and utilize donor resources. Flexible funding provides greater discretion in expenditure, resource allocation, and budget adjustments, while restrictive conditions may limit organizational autonomy and responsiveness (UNHCR, 2024; Smillie, 2001).

Although previous studies have examined donor funding in relation to NGO sustainability, accountability, and financial performance, limited empirical attention has focused specifically on the effect of funding flexibility on funds utilization efficiency. Evidence on this relationship among NGOs in Nairobi also remains limited. Therefore, this study examines the effect of donor funding flexibility on the financial performance of NGOs in Nairobi, Kenya, using funds utilization efficiency as the measure of financial performance.

RESEARCH OBJECTIVE

To examine the effect of donor funding flexibility on the financial performance of Non-Governmental Organizations (NGOs) in Nairobi, Kenya.

RESEARCH QUESTION

What is the effect of donor funding flexibility on the financial performance of Non-Governmental Organizations (NGOs) in Nairobi, Kenya?

THEORETICAL REVIEW

Agency Theory

This study was anchored on Agency Theory, developed by Jensen and Meckling (1976) to explain the relationship between principals and agents. In donor-funded NGOs, donors act as principals by providing financial resources, while NGOs act as agents responsible for utilizing these resources to achieve agreed development objectives. The theory posits that monitoring mechanisms and accountability structures help align the interests of principals and agents and ensure resources are utilized for their intended purposes (Jensen & Meckling, 1976). In the NGO sector, donor controls often take the form of funding restrictions, expenditure conditions, reporting requirements, and approval procedures. While these mechanisms enhance accountability, excessive controls may limit organizational flexibility and decision-making. Wallace, Bornstein and Chapman (2006) observed that restrictive donor requirements can reduce the ability of NGOs to adapt programs and allocate resources in response to changing operational realities. Similarly, Smillie (2001) found that rigid funding arrangements may limit local ownership and organizational responsiveness.

The Theory further suggests that agency costs arise when the principal and agents' interests are not fully aligned. In donor-funded programs, donors may emphasize compliance and accountability, whereas NGOs may seek greater flexibility to address beneficiary needs and contextual realities (Jensen & Meckling, 1976). Consequently, restrictive funding conditions may divert resources toward compliance activities and reduce operational efficiency (Burger & Owens, 2010).

The theory is particularly relevant to funding flexibility because it explains how donor funding conditions influence organizational performance. Funding arrangements that provide reasonable flexibility enable NGOs to reallocate resources, adjust budgets, and make timely decisions while maintaining accountability. Such flexibility enhances organizational responsiveness and supports efficient resource utilization (Smillie, 2001). Pfeffer and Salancik (1978) similarly argue that organizations perform more effectively when they can manage dependencies on external resource providers and exercise discretion in resource allocation. Empirical evidence further suggests that balancing accountability with flexibility is essential for effective resource utilization (Burger & Owens, 2010). Consequently, Agency Theory provides an appropriate lens for examining the relationship between donor funding flexibility and financial performance among NGOs.

Funding Flexibility and Financial Performance

Funding flexibility refers to the extent to which donor funding is provided with minimal restrictions, allowing recipient organizations discretion in allocating and utilizing resources according to organizational priorities and operational needs (UNHCR, 2024). Such arrangements may include unrestricted funding, budget reallocations, and the ability to adapt program activities in response to changing circumstances, enabling NGOs to respond effectively to emerging needs. Within the NGO sector, funding flexibility is increasingly recognized as an important determinant of organizational effectiveness and performance. NGOs operate in dynamic environments characterized by evolving program priorities, and uncertain implementation conditions. Banks, Hulme, and Edwards (2015) argue that NGOs require sufficient operational autonomy to remain responsive and relevant, while Wallace, Bornstein and Chapman (2006) observed that rigid donor requirements may constrain decision-making and reduce program effectiveness. Funding flexibility enables organizations to allocate resources where they are most needed, adjust implementation strategies, and address unforeseen operational challenges. Smillie (2001) noted that organizations operating under flexible funding arrangements are better positioned to align resource allocation with operational realities.

Financial performance within the nonprofit sector is commonly assessed through the efficient utilization of available resources rather than profit generation (Mureithi, 2019). In this study, financial performance is measured using funds utilization efficiency, which refers to the extent to which donor resources are utilized in accordance with approved budgets, implementation timelines, donor requirements, and intended program objectives. Efficient utilization of donor funds strengthens accountability, minimizes wastage, and improves the effectiveness of development interventions (Teegen, Doh, & Vachani, 2004). The relationship between donor funding flexibility and financial performance is based on the premise that organizations require sufficient discretion in resource allocation to respond effectively to operational realities. Flexible funding arrangements enable NGOs to redirect resources to priority activities, manage implementation risks, and address emerging needs without unnecessary delays. As a result, organizations operating under flexible donor arrangements are expected to achieve better financial performance through more efficient utilization of donor resources.

EMPIRICAL REVIEW

Several studies have examined the relationship between donor funding arrangements and organizational performance. Smillie (2001) found that restrictive donor conditions limit organizational autonomy and reduce the ability of NGOs to allocate resources according to contextual needs, while greater funding flexibility enhances organizational responsiveness and resource utilization. However, the study focused on humanitarian capacity building rather than funds utilization efficiency. Burger and Owens (2010) established that stringent donor reporting and compliance requirements increase administrative burdens and divert organizational resources away from program implementation activities. Although the findings highlighted the effects of restrictive donor requirements, the study focused primarily on transparency and financial disclosure.

In Kenya, Miriti and Karithi (2020) found that NGOs operating under flexible funding arrangements demonstrated stronger financial management practices. Similarly, Mureithi (2019) reported that favorable donor funding arrangements enhance planning, budgeting, implementation effectiveness, and overall organizational performance. However, neither study specifically examined funds utilization efficiency as a financial performance outcome. Nato and Gaiku (2022) found that favorable donor funding structures positively influence organizational performance by enhancing financial stability and operational effectiveness. Likewise, Kariega (2020) established that supportive funding arrangements contribute to improved project implementation and operational performance among NGOs. Nevertheless, both studies focused on broader performance outcomes rather than funds utilization efficiency.

The reviewed studies suggest that funding flexibility enhances organizational responsiveness, financial management, and overall performance. However, limited empirical attention has been given to funds utilization efficiency as a distinct financial performance outcome, particularly among NGOs operating in Nairobi. This gap provides the basis for examining the relationship between donor funding flexibility and financial performance among NGOs in Nairobi, Kenya.

CONCEPTUAL FRAMEWORK

Kothari and Garg (2020) argue that a conceptual framework provides a diagrammatic representation of the relationships between the independent and dependent variables in a study. In the present study, the conceptual framework illustrates the hypothesized relationship between donor funding flexibility and the financial performance of non-governmental organizations (NGOs) in Nairobi, Kenya. Donor funding flexibility constitutes the independent variable and is operationalized in terms of flexibility in expenditure management, availability of unrestricted funds, allocation of resources to priority needs, adjustments in resource utilization, and flexibility in budget modifications. Financial performance constitutes the dependent variable and is measured in terms of funds utilization efficiency. The framework posits that greater flexibility in donor funding enables NGOs to allocate and utilize financial resources more efficiently in response to organizational priorities and emerging needs, thereby enhancing their financial performance.

Independent Variable **Dependent Variable**

Donor Funding Flexibility
- Expenditure management
- Unrestricted funds
- Allocation to priority program needs
- Adjustments to changing needs
- Budget modifications

→

Financial Performance
- Funds utilization efficiency

Figure 1: Conceptual Framework

RESEARCH METHODOLOGY

The study adopted a descriptive research design to examine the effect of donor funding flexibility on the financial performance of Non-Governmental Organizations (NGOs) in Nairobi, Kenya. Financial performance was measured using funds utilization efficiency. The target population comprised 71 NGOs registered with the Non-Governmental Organizations Co-ordination Board, identified as leading organizations in funds receipt and utilization. Using Yamane's (1967) formula at a 95% confidence level, a sample of 60 NGOs was selected. The study targeted executive managers, finance managers, accountants, and program managers due to their direct involvement in donor funding management and financial oversight. A total of 240 respondents was selected from whom 211 responses were obtained.

Primary data was collected using structured questionnaires, while secondary data was obtained from reports published by the NGO Board. The collected data was analyzed using the SPSS. Descriptive statistics were used to summarize the data, while Pearson correlation and simple linear regression analyses were used to determine the relationship between donor funding flexibility and financial performance. Analysis of variance (ANOVA) was used to assess the significance of the regression model.

The study adopted the following empirical model:

$$Y = \beta_0 + \beta_1 X_1 + \varepsilon$$

Where:

Y = Financial Performance (measured by Funds Utilization Efficiency)

β_0 = Constant

X_1 = Donor Funding Flexibility

β_1 = Regression Coefficient

ε = Error Term

The model was used to determine the effect of donor funding flexibility on the financial performance of NGOs in Nairobi, Kenya.

RESEARCH FINDINGS AND DISCUSSION

A total of 240 respondents comprising executive managers, finance managers, accountants, and program managers from selected Non-Governmental Organizations (NGOs) in Nairobi, Kenya, were targeted for the study. Of the 240 questionnaires distributed, 211 were successfully completed and returned, representing a response rate of 87.9%. This response rate was considered adequate for descriptive and inferential statistical analysis and provided sufficient representation of the target population. The results presented in this article relate to the study objective that examined the effect of donor funding flexibility on the financial performance of NGOs in Nairobi, Kenya. Financial performance was measured using funds utilization efficiency. The analysis includes descriptive statistics on donor funding flexibility and financial performance, as well as correlation and regression analyses to determine the nature, strength, and statistical significance of the relationship between the two variables.

Descriptive Statistics For Funding Flexibility

Funding flexibility was measured using five indicators relating to flexibility in expenditure management, availability of unrestricted funds, allocation of resources to priority program needs, adjustments in resource utilization, and flexibility in modifying budget lines during program implementation. Responses were measured using a five-point Likert scale ranging from 1 = Strongly Disagree to 5 = Strongly Agree.

Table 1: Descriptive Statistics on Donor Funding Flexibility

Statement	N	Mean (M)	Std. Deviation (SD)
Donor funding terms in our organization allow flexibility in the management of expenditures.	211	3.99	0.80
A portion of donor funds received by our organization is unrestricted in its use.	211	4.08	0.81
Donor funding requirements allow us to allocate resources to priority program needs in our organization.	211	4.11	0.74
Our donor funding conditions allow adjustments in resource utilization in response to changing community needs.	211	3.98	0.77
The donor funding terms allow us to adjust the budget lines during program implementation.	211	4.10	0.77
Overall Mean		4.04	0.78

The findings indicate that respondents generally agreed that donor funding arrangements provide a considerable degree of flexibility (M = 4.04, SD = 0.78). This suggests that the sampled NGOs, which were identified by the Non-Governmental Organizations Co-ordination Board as among the leading organizations in fund receipt and utilization, operate under funding conditions that allow reasonable discretion in expenditure management, resource allocation, and program implementation. The relatively low standard deviations further indicate consistency in respondents' responses. The highest mean score was recorded for the statement that donor funding requirements allow resources to be allocated to priority program needs (M = 4.11, SD = 0.74), followed by flexibility in adjusting budget lines during program implementation (M = 4.10, SD = 0.77). Respondents also agreed that a portion of donor funds received by their organizations is unrestricted in its use (M = 4.08, SD = 0.81). In addition, donor funding terms were perceived to allow flexibility in expenditure management (M = 3.99, SD = 0.80) and adjustments in resource utilization in response to changing program or community needs (M = 3.98, SD = 0.77).

Descriptive Statistics on Financial Performance

Secondary data was obtained to assess the rate of funds utilization, calculated as the proportion of funds utilized relative to funds received over the period 2020-2024. The data provided an objective measure of funds utilization efficiency among NGOs in Nairobi.

Table 2: Trend in Funds Utilization Efficiency

Year	Funds Received	Funds Utilized	Utilization Rate
2020-2021	62,569,442,985	37,637,795,251	60.15%
2021-2022	81,638,438,315	57,906,690,217	70.93%
2022-2023	84,453,870,042	51,865,256,235	61.41%
2023-2024	87,639,538,091	55,398,595,189	63.21%
Overall			**63.86%**

The findings indicate that the funds utilization rate among the sampled NGOs ranged from 60.15% to 70.93% during the study period. In 2020/2021, the sampled NGOs received KES 62.57 billion and utilized KES 37.64 billion, resulting in a utilization rate of 60.15%. The utilization rate increased to 70.93% in 2021/2022 before declining to 61.41% in 2022/2023 and slightly improving to 63.21% in 2023/2024. The overall funds utilization rate for the study period was 63.86%.

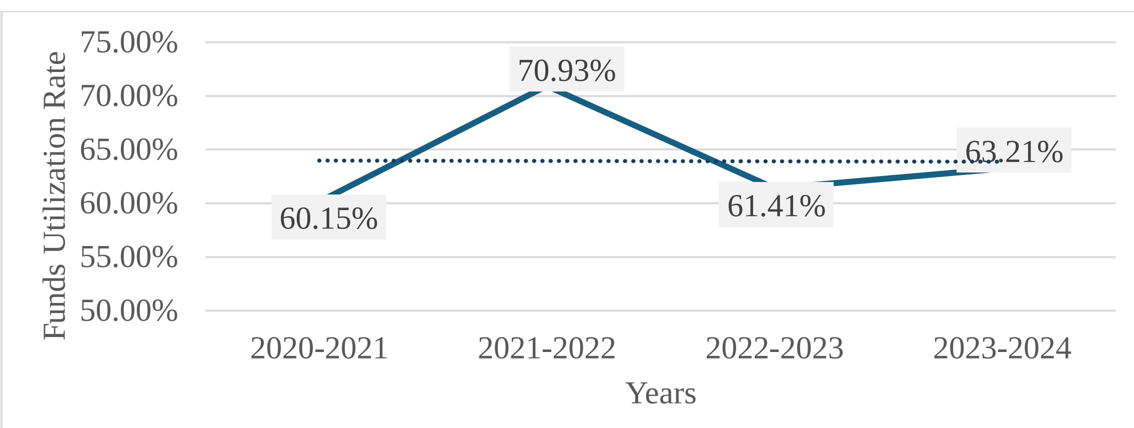

Figure 1: Rate of Funds Utilization Trend

The findings indicate that although the sampled NGOs utilized a substantial proportion of donor resources, a considerable share remained unutilized. The observed variations in utilization rates suggest that funds utilization efficiency is influenced by organizational and funding-related factors. These findings provide objective evidence of differences in funds utilization efficiency and support further examination of funding flexibility as a determinant of efficient donor resource utilization.

Correlation Analysis for Funding Flexibility and Financial Performance

Pearson correlation analysis was conducted to determine the association between funding flexibility and financial performance among NGOs in Nairobi.

Table 3: Correlation Analysis for Funding Flexibility and Financial Performance

Variable	Financial Performance
Funding Flexibility	0.740
Sig. (2-tailed)	0.000

The findings indicate a positive and significant relationship between funding flexibility and financial performance ($r = 0.740$, $p < 0.01$). Financial performance, measured through funds utilization efficiency, was positively associated with funding flexibility. This suggests that NGOs operating under flexible donor funding arrangements are more likely to utilize donor resources efficiently. Flexibility in expenditure management, resource allocation, budget adjustments, and the use of unrestricted funds may enhance the ability of organizations to respond to operational needs and utilize resources effectively. The findings support Agency Theory, which suggests that excessive funding restrictions may constrain organizational autonomy and operational efficiency. They are also consistent with Smillie (2001), who found that flexible donor funding enables organizations to align resources with program priorities, and Miriti and Karithi (2020), who reported that flexible funding arrangements strengthen financial management and resource utilization. The positive correlation provides preliminary evidence that funding flexibility is associated with improved financial performance. However, correlation analysis only establishes association; therefore, regression analysis was conducted to determine the effect of funding flexibility on financial performance.

Regression Analysis for Funding Flexibility and Financial Performance

To determine the effect of funding flexibility on financial performance among NGOs, a simple linear regression model was fitted. The results of the model summary, analysis of variance (ANOVA), and regression coefficients are presented below.

Table 4: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.740	0.548	0.546	0.263

a. Predictors: (Constant), Funding Flexibility

The results indicate a strong positive relationship between funding flexibility and financial performance ($R = 0.740$). The coefficient of determination ($R^2 = 0.548$) indicates that funding flexibility explains approximately 54.8% of the variation in financial performance among NGOs in Nairobi. The adjusted R^2 value of 0.546 further confirms the stability of the model. These findings suggest that funding flexibility is an important determinant of financial performance and makes a substantial contribution to explaining variations in donor resource utilization among NGOs.

Table 5: ANOVA

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	9.569	1	9.569	137.915	0.000
	Residual	15.201	209	0.073		
	Total	24.770	210			

The ANOVA results indicate that the regression model is statistically significant, $F(1, 209) = 137.915$, $p < 0.001$. This suggests that funding flexibility is a significant predictor of financial performance among NGOs in Nairobi. The findings further confirm that the relationship between funding flexibility and financial performance is unlikely to have occurred by chance.

Table 6: Regression Coefficients for Funding Flexibility and Financial Performance

Variable	B	Std. Error	Beta	t	Sig
Constant	1.374	0.189	-	7.270	0.000
Funding Flexibility	0.353	0.066	0.483	5.354	0.000

The regression results indicate that funding flexibility has a positive and statistically significant effect on financial performance, measured through funds utilization efficiency ($\beta = 0.483$, $t = 5.354$, $p < 0.001$). The findings suggest that NGOs operating under flexible donor funding arrangements are more likely to utilize donor resources efficiently. The unstandardized coefficient ($B = 0.353$) indicates that a one-unit increase in funding flexibility leads to a 0.353-unit increase in financial performance, holding other factors constant. The findings support Agency Theory, which posits that excessive donor controls may constrain organizational autonomy and resource allocation. Conversely, flexible funding arrangements provide organizations with greater discretion in managing resources, enabling timely decision-making while maintaining accountability. Such flexibility enhances the efficient utilization of donor resources and improves financial performance.

The findings are consistent with Smillie (2001), who observed that flexible funding arrangements enhance organizational responsiveness and resource allocation. Similarly, Miriti and Karithi (2020) found that less restrictive donor funding arrangements contribute to stronger financial management and improved organizational performance. The current study extends these findings by demonstrating that donor funding flexibility significantly influences financial performance among NGOs in Nairobi, Kenya. Overall, the findings provide empirical evidence that donor funding flexibility is a significant determinant of financial performance. Donor funding arrangements that provide reasonable discretion in resource allocation and expenditure management can enhance the efficient utilization of donor resources and improve program implementation outcomes.

The regression model can therefore be expressed as:

$Y = 1.374 + 0.353X_1 + \varepsilon$

Where:

Y = Financial Performance (measured by Funds Utilization Efficiency)

X_1 = Funding Flexibility

1.374 = Constant

0.353 = Regression coefficient of Funding Flexibility

ε = Error Term

The model indicates that increases in donor funding flexibility are associated with corresponding improvements in financial performance among NGOs. This underscores the importance of donor funding arrangements that provide adequate discretion in expenditure management, resource allocation, and program implementation.

CONCLUSION

This study examined the effect of donor funding flexibility on the financial performance of Non-Governmental Organizations (NGOs) in Nairobi, Kenya, measured using funds utilization efficiency. The findings established that donor funding flexibility has a positive and significant effect on financial performance. NGOs operating under flexible funding arrangements were better able to allocate resources to priority activities, adjust expenditures to emerging needs, and respond to changing operational conditions. The study concludes that donor funding flexibility is an important determinant of financial performance among NGOs. Funding arrangements that balance flexibility and accountability enhance the efficient utilization of donor resources and support effective program implementation.

RECOMMENDATIONS

The study recommends that donor agencies adopt more flexible funding arrangements that provide NGOs with reasonable discretion in resource allocation and expenditure management while maintaining appropriate accountability mechanisms. Such arrangements can enhance organizational responsiveness and improve financial performance.

NGOs should strengthen internal financial management systems to ensure that available funding flexibility is utilized effectively, transparently, and in line with organizational priorities. Strong financial controls can enhance the efficient utilization of donor resources and support improved financial performance.

Future studies should examine the effect of donor funding flexibility on financial performance in different geographical and organizational contexts to determine the extent to which the findings are generalizable.

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