THE RELATIONSHIP BETWEEN CASH FLOW MANAGEMENT AND THE FINANCIAL PERFORMANCE OF NGOs IN KENYA: CASE OF NGOs IN NAIROBI.

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DECLARATION

This Research Project is my original work and has not been presented to any other University for academic award.

Signed: ___________________________ Date: __________ 2011

Henry Kissinger Kimonge

D61/70981/2007

This Research Project has been submitted for examination with my approval as the University Supervisor.

Signed: ___________________________ Date: __________

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Chairman: Department of Finance & Accounting, University of Nairobi.
DEDICATION

This work is dedicated to my late grandfather and my grandmother for their love, care, support and prayers.
ACKNOWLEDGEMENT

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ABSTRACT

The study sets out the relationship between cash flows management and financial performance indicators of NGOs operating in Nairobi and who file audited financial reports with the NGOs Coordination Board.

The financial statements for NGOs operating in Nairobi were obtained from the records and database of the NGOs Coordination Board for the years 2006 and 2010. From the data extracted from the financial statements and the database, an in-depth analysis involving simple and multiple regression were performed with the aid of the statistical package for social sciences (SPSS) version 19 to establish the relationship between cash flows management and the financial performance as indicated by the fiscal performance ratio.

The concept of financial performance among NGOs is relatively a new one and the study identifies critical areas that need further research to firm up on the ways of measuring the financial performance of NGOs.

The regression results displayed no significant relationship between cash flows management and the financial performance of the NGOs registered by the NGOs coordination Board and operating in Nairobi.
1.1 Background to the Study

The one unifying consideration all organizations share, whether publicly held, privately held, government or not for profit, is the concern over liquidity management. It is a safe assumption that for-profit entity will not remain in business long if it either lacks liquidity or does not effectively manage its liquidity. Similarly, a not for-profit organization cannot continue to meet its mission objectives, or at the very least risk jeopardizing its relationships with its stakeholders if it lacks prudent liquidity management. In short liquidity management is a major concern for every organization (Zietlow, 2007)

The recent financial crisis has put cash and its management back in the spotlight, forcing treasurers to focus their efforts on ways to improve their companies’ cash management (Bergen, 2006). When liquidity is scarce efficient cash management is vital for ensuring that every spare cent has been fully utilized. Dropkin & Hayden (2001) state that efficient cash management is crucial for any company, as lack of liquidity may result in inability to pay liabilities, increased costs, and worst case scenario, the company may end up in insolvency.

According to Harford (2000), if cash flows and liquid funds are not effectively and successfully planned and managed, a company may not be able to pay its suppliers and employees in a timely manner. It may be profitable according to its financial statements, but in fact, the company will not be able to pay its obligations when they come due. Moreover, lack of liquidity will incur increased costs in the form of interest charges on loans, late payment penalties and losing supplier discounts for paying obligations on time. Proper cash management can avoid the costs of additional funding and can provide the opportunity for more favorable terms of payment (Dropkin & Hayden, 2001).

Cash is crucial for every business (Coyle, 2000). Every company has to have cash on hand or at least access to cash in order to be able to pay for the goods and services it uses, and consequently, to stay in business (Harford, 2000). By ensuring the company with the necessary
funds for supporting its everyday operations, cash management becomes a vital function for the company. According to Harford (2000), cash flows have an impact on the company’s liquidity. Liquidity is the ability of the company to pay its obligations when they come due. It is comprised of: cash on hand, assets readily convertible into cash, as well as ready access to cash from external sources, such as bank loans (Coyle, 2000).

Cash flow is also referred to as the measure of your ability to pay your bills on a regular basis (Hughes, 2007). It depends on the timing and amounts of money flowing into and out of the business each week and month. Good cash flow means that the pattern of income and spending in a business allows it to have cash available to pay bills on time. Fabozzi & Peterson, (2003) state that the available cash includes: coins and notes, money in current accounts and short-term deposits, any unused bank overdraft facility and foreign currency and deposits that can be quickly converted to your currency. It does not include: long-term deposits, money owed by customers and stock.

Cash management has the following purposes: controlling spending in the aggregate, implementing the budget efficiently, minimizing of the cost of government borrowing, and maximizing the opportunity cost of resources (Fabozzi & Peterson, 2003). Control of cash is a key element in macroeconomic and budget management. However, it must be complemented by an adequate system for managing commitment (Foster, 1997). It is necessary to minimize transaction costs and to borrow at the lowest interest rate or to generate additional cash by investing in revenue-yielding paper. According to Coyle (2000), it is also necessary to avoid paying in advance and to track accurately the dates on which payments are due.

Cashflow management is the process of monitoring, analyzing, and adjusting business’ cashflows (Dropkin & Hayden, 2001). Cash flow is the lifeblood of all businesses and is the primary indicator of business health.

According to Foster (1997), during the business cycle, there will be more money flowing in than flowing out. This will allow you to build up cash balances with which to plug cash flow gaps, seek expansion and reassure lenders and investors about the health of your business. Fabozzi & Peterson, (2003) state that management of cash flows is very vital to the operations of any
organization as it must remain liquid enough to be able to finance its short-term or immediate obligations. The management of cash flows must be in such a manner that the liquid cash is not in excess but must be balanced against the fixed assets. This means that the sources of finances and the application must be carefully managed (Hughes, 2007).

1.1.1 Financial Performance of Nonprofit Organizations

Anthony, et al (1994) financial management of not-for-profits is similar to financial management in the commercial sector in many respects; however, certain key differences shift the focus of a not-for-profit financial manager. A for-profit enterprise focuses on profitability and maximizing shareholder value. A not-for-profit organization’s primary goal is not to increase shareholder value; rather it is to provide some socially desirable need on an ongoing basis. A not-for-profit generally lacks the financial flexibility of a commercial enterprise because it depends on resource providers that are not engaging in an exchange transaction. The resources provided are directed towards providing goods or services to a client other than the actual resource provider. Thus the not-for-profit must demonstrate its stewardship of donated resources — money donated for a specific purpose must be used for that purpose. That purpose is either specified by the donor or implied in the not-for-profit’s stated mission. The management and reporting activities of a not-for-profit must emphasize stewardship for these donated resources. Budgeting and cash management are two areas of financial management that are extremely important exercises for not-for-profit organizations.

Why is financial performance of nonprofit organizations important? First, nonprofit organizations have substantial employment impacts. In 2001, the number of employed persons in nonprofit organizations was already approximately 12.5 million (www.colliers.com/). If many nonprofit organizations are under financial vulnerability, they may have to cut the number of staff members, as well as their service offerings. Thus, the financial performance of nonprofit organizations has significant impacts on employments. Also, reducing service offerings to respond to financial pressures will increase the demand for delivering those services by the government. This situation might increase the government’s expenditures to deliver those services. Or, if the government does not deliver those services, people will have to live without the services.
According to Shinwoo (2010) financial performance of all nonprofit organizations is measured by three sub-financial performance ratios: fiscal performance, fundraising efficiency, and public support ratio. First, the fiscal performance ratio shows the fiscal-management status of each organization, and this category is calculated as the ratio of total revenues to total expenses (Siciliano, 1997). Second, the fundraising efficiency ratio measures the relationship between fundraising costs and total contributions and indicates the amount of contributions raised for each dollar of fundraising cost incurred (Greenlee and Bukovinsky, 1998). Third, the public support ratio indicates the extent of an organization’s dependency on direct public support and is calculated as the ratio of total contributions divided by total revenue (Shinwoo, 2010).

As non-governmental organizations continue to increase in size, quantity, and impact financial management will continue to play one of the most important role in the organization to ensure that it is fully effective towards its goals and objectives of its mission (Fisher, 1998).

1.1.2 NGOs in Kenya

NGOs Co-ordination Act 1990 defines a Non-Governmental Organization (NGO) as a private voluntary grouping of individuals or associations not operated for profit or other commercial purposes but which have organized themselves nationally or internationally for the benefit of the public at large and promotion of social welfare, development, charity or research in the areas inclusive of, but not restricted to health, agriculture, education, industry and supply of amenities and services (National Survey of NGOs Report, 2009).

According to Wikipedia encyclopedia, a non-governmental organization is a non-profit group or association that acts outside the institutionalized political structures and pursues matters of interest to its own members by lobbying, persuasion or direct actions. The term is generally restricted to social, cultural, legal and environmental advocacy groups having goals that are primarily non-commercial. NGOs gain at least a portion of their funding from private sources. Because the label “NGOs” is considered too broad by some, as it might cover anything that is non-governmental, many NGOs now prefer the term private voluntary organizations (PVO) or Private Developmental Organizations (PDO). Different sources refer to these groups with different names, using NGOs, Civil Society Organizations (CSO), PVO, Charities, nonprofit
charities, charitable organizations, third sector organizations, and so on. These groups can encompass a wide variety of groups from corporate-funded think tanks, community groups, grass root activist groups, development and research organizations, advocacy groups, operational, emergency/humanitarian relief focused, and so on. While there may be a distinction in specific situations, this section deals with a high level look at these issues, and so these terms may be used interchangeably, and sometimes using NGOs as the umbrella term (World Bank, 1995).

NGOs carry out various activities/projects towards the fulfillment of their objectives. Related activities are usually grouped based on their thematic relationships referred to as sectors. While a number of organizations carry out integrated programmes (i.e. combine a number of different activities under one project i.e. HIV/AIDS, Microfinance, Agriculture, etc) they would normally have a core focus for instance mitigation of the impact of HIV/AIDS which would then make such a project fall in the HIV/AIDS sector (National Survey of NGOs Report, 2009).

According to the National Survey of NGOs Report (2009), the last decade has witnessed substantial growth in the number of organizations registered under the NGOs Co-ordination Act of 1990. The sector recorded significant growth between 2001 and 2007 which could be attributed to the impact of globalization and the opening up of democratic space in Kenya. Since 2001, the sector has been growing at the rate of 400 organizations per year. By August 2009, the board had cumulatively registered 6,075 organizations (Mostashari, 2005).

1.2 Statement of the Problem

The management of cash flow is crucial for effectiveness of operations in any organization. Non-governmental organizations get their funds from the donor community, well wishers and the subscriptions from the members (Fisher, 1998: Mostashari, 2005). Cash inflows and outflows are the heartbeat of every business. One of the main reasons that business fail is their inability to meet their financial obligations when they fall due as they have run out of cash. Knowing how to maintain a healthy cash flow is essential to a successful business. A lack of cash flow data has caused problems for investors and analysts in assessing a company’s performance, liquidity, finance flexibility and operating capability (Figlewicz & Zeller, 1991). Liquidity policy and practice has almost been totally overlooked in nonprofit management periodicals. Notable
exceptions are (Wacht, 1984) who notes that growing donative human services organization require access to liquid reserves to cope with cash flow problems. First, nonprofit managers, employees, and board members commonly lament the perennial cash crunch or ongoing cash crises faced by other organizations (Hall, 1995). Second, this area of financial management is one that shares very much in common with business (Phillips, 1997). Ritchie and Kolodinsky (2003), there has not been enough empirical research to show the confidence in measuring financial performance of nonprofit organizations, while the importance of financial performance has been emphasized continuously. The question that this study seeks to answer is: What is the relationship between cash flow management and financial performance of NGOs in Nairobi?

The chief financial officers of most companies spend most of their time and effort on day-today working capital management. Still, due to the inability of financial managers to properly plan and control the current assets and current liabilities of their companies, the failure of a large number of businesses can be attributed to the inefficient working capital management (Smith, 1973).

Specific studies exclusively on the relationship between cash flows management and financial performance of NGOs are scanty, especially for the case of Kenya. Related local studies on but in the private sector include, Kiprono (2004) on the relationship between cash flow and earnings performance measures for companies listed on the Nairobi Stock Exchange. And Abunga (1977) did a research on the funds flow statements and user needs in Kenya. Whilst these earlier studies have focused on the private sector in Kenya, this study focuses on the Non-Governmental Organizations sector in Kenya and specifically looks at the relationship between cash flows management and financial performance. Also Nzalu (2000) undertook a study on the financial practices among development NGOs in Kenya. Again this study goes beyond financial practices to establish the relationship between cash flow management and financial performance of NGOs in Kenya using fiscal performance ratio as the measurement indicator. Therefore, this study is a modest attempt on the topic under discussion and the results are expected to contribute to the existing literature on cash flows management and finance performance of NGOs.
1.3 Objective of the Study
To establish the relationship between cash flow management and financial performance of nongovernmental organizations in Kenya.

1.4 Significance of the Study
The study will be of value to various interest groups including:

The management and board of directors of the NGOs will find this study helpful in identifying cash flow management policies that will improve their financial performance. Improved financial performance will translate into increased donor funding and efficient and effective achievement of their scopes of work or program deliverables. Donor funding normally come after thorough review of the organizations ability to manage such funds, account for the funds and the level of attainment of the past scopes of work as agreed in the various agreements or memorandum of understanding with the recipients.

The regulators and the policy makers can use the finding as reference for policy guidelines on management and control of such organizations. They will be able to use the findings of the study to formulate viable policy documents that effectively address problems faced by the nongovernmental organizations. These may relate to regulating those aspects that threaten to adversely impact on the operations and development of such organizations, for example, NGOs Coordination Board and the Ministry of Culture and Social Services of the Government of Kenya.

The study will enable the donors assess the capability of the non-governmental organization in managing their funds in transparent and efficient way. Due to information asymmetry, managers may use their discretion to benefit their private interest in a variety of ways including empire building. A statement of cash flows will be a critical tool for analysis and forming informed decisions of the effectiveness of cash flow management before releasing additional funding to the nongovernmental organizations.
The study will provide additional information into the already existing body of literature regarding the factors affecting cash flow management and how they impact on the financial performance of non-profit making organizations. Nonprofit organizations have substantial employment impacts. If many nonprofit organizations are under financial vulnerability, they may have to cut the number of staff members, as well as their service offerings. Thus, the financial performance of nonprofit organizations has significant impacts on employments.

Also, reducing service offerings to respond financial pressures will increase the demand for delivering those services by the government. This situation might increase the government’s expenditures to deliver those services. Or, if the government does not deliver those services, people will have to live without the services. Again, the government will find this study useful in determining how and when to intervene to save NGOs from imminent collapse or by creation of an enabling environment for the NGOs to thrive.
CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction
This chapter summarizes the information from other researchers who have carried out research in similar fields of study. The specific areas covered here are review of literature on theories that guide the study, the empirical studies that relate to the study, financial performance and cash flow management review and lastly the summary of the whole chapter.

2.2 Theoretical Reviews

2.2.1 Accrual Theory of Accounting
The concept is also known as accrual theory of accounting or accrual accounting. This concept applies equally to revenues and expenses. In the accrual basis of accounting revenue is recognized when it is realized, that is, when the sale is completed. Similarly, the expenses are recognized in the accounting period in which they assist in earning the revenues, whether the cash has been paid for them or not. Recognition of revenues and expenses for income determination therefore does not depend upon the time when the cash is actually received for the expenses or paid for expenses. The essence of revenue is that a mere promise on the part of a customer to pay the money for the sale or service or interest, commission, rent, etc in future is considered as revenue. Similarly, a promise on the part of the business entity to make payment for salaries, rent, etc in future is considered as an expense. Income (excess of revenue - expenses) is associated with the change in the owner's equity and that is not necessarily related to changes in cash (transtutors.com)

According to Dechow, et al., (2002) it is important to have a measure of one aspect of the quality of working capital accruals and earnings. The measure is based on the observation that accruals shift or adjust the recognition of cash flows over time; so that the adjusted numbers (earnings), better measure firm performance. For example, recording a receivable accelerates the recognition of a future cash flow in earnings, and matches the timing of the accounting recognition with the timing of the economic benefits from the sale. However, accruals are frequently based on
assumptions and estimates that, if wrong, must be corrected in future accruals and earnings. For example, if the net proceeds from a receivable are less than the original estimate, then the subsequent entry records both the cash collected and the correction of the estimation error. We argue that estimation errors and their subsequent corrections are noise that reduces the beneficial role of accruals. Therefore, the quality of accruals and earnings is decreasing in the magnitude of accrual estimation errors. Our empirical measure of accrual quality is the extent to which working capital accruals map into operating cash flow realizations, where a poor match signifies low accrual quality.

Accrual basis accounting better shows a period’s operating results by virtue of the fact it has revenues recorded when earned and expenses are recorded when incurred. The biggest downfall of accrual basis accounting, which is mandated by GAAP, is that it may not portray how your organization’s cash position is changing. This is the reason why emphasis is placed on the statement of cash flows (Zietlow, 2007).

2.2.2 Trade Credit Theory

It is typically less profitable for an opportunistic borrower to divert inputs than to divert cash. Therefore, suppliers may lend more liberally than banks. This simple argument is at the core of our contract theoretic model of trade credit in competitive markets. The model implies that trade credit and bank credit can be either complements or substitutes. Among other things, the model explains why trade credit has short maturity, why trade credit is more prevalent in less developed credit markets, and why accounts payable of large unrated firms are more countercyclical than those of small firms (Burkart, et al 2004)

Trade credit is a short-term credit facility extended by suppliers of raw materials and other suppliers in the normal course of business (Dropkin & Hayden, 2001). It is a common and important source of financing. Either open account credit or acceptance credit may be adopted. In the former as per business custom credit is extended to the buyer, the buyer is not signing any debt instrument as such. The invoice is the basic document. In the acceptance credit system, a bill of exchange is drawn on the buyer who accepts and returns the same. The bill of exchange evidences the debt. Trade credit is an informal and readily available credit facility. It is
unsecured. It is also flexible in the sense that advance retirement or extension of credit period can be negotiated. But trade credit may be costlier as the supplier may inflate the price to account for the loss of interest for delayed payments, although this method of credit does not involve explicit interest charge. If the company has liquidity difficulties, it may be able to stretch accounts payable; however the company will be required to give up any cash discount offered and accept a lower credit rating (Coyle, 2000).

Chittenden et al (1998) reported that granting of credit has existed as long as trade itself. They also state that trade credit is an important source of short-term finance because it represents a substantial component of the business assets and liabilities for the small business. In their findings they found that more than 96 per cent of small businesses provide credit to their customers. In addition, the impact of trade debtors and trade creditors after the introduction of the GST (Goods and Services Tax) has had a compounding effect on cash management practices. McMahon and Holmes (1991) found that owner-managers tend to neglect accounts receivable management and that it is exogenously determined and beyond their active control. On the other hand, Chittenden et al, (1998) reported that management of accounts receivable is paramount to the survival and success of every business.

2.2.3 Agency Theory

Agency theory motivates us to better understand organizational liquidity. The argument is that managers build excess liquidity, or slack, because they are overly concerned about risk. For businesses, managerial risk aversion exceeds stockholder risk aversion, because stockholders are well diversified. The same argument may extend to donative non-profits organizations. To the extent that they are multiple organizations engaging in similar services (and with the same or very similar values and philosophies), the probability of organization’s failure and dissolution is of less concern to donors than the organization’s managers. Donors may simply reallocate donations to surviving organizations when one of the existing fails (Zietlow, 2007).

This theory is very relevant to the member subscriptions and donor funds as a source of cash for the NGOs. According to Freedman, (2008), voluntary organizations are being forced to be more accountable for the manner in which they spend their resources. Donors have become more
restrictive with funding. General-purpose grants from major donors and foundations have been reduced. More grants now come with both financial and programmatic restrictions. Increasingly, grants are being restricted for specific program purposes. This limits the amount that grantees can spend to support operations.

Funders have also increased the reporting requirements. Grantees are more frequently asked to provide detailed financial and programmatic reviews. The financial reports are organized by budget categories thereby reducing the grantee's ability to spend these funds on non-grant programs. These restrictions, that is, grants that limit expense allocations, have forced voluntary organizations to be more focused on the efficiency of their operations. Overall, this improved accountability has resulted in more streamlined organizations that focus on community needs (Freedman, 2008).

Zietlow (2007) grantors have also become more restrictive in limiting the overhead costs that they are willing to reimburse. NPO's (not for-profit organizations) are therefore faced with the issue of controlling their indirect costs or losing money (the difference between the rate provided by the grantor and the organization's actual rate) on foundation grants. Given this prospect, grantees have become more diligent in controlling indirect costs.

2.3 Empirical Studies

Allen and Cote (2005) in their study on creditors' use of operating cash flows have found that investors and creditors differing goals offer initial clues to differences in their decision-making behavior. Investors are the residual owners and their returns are limited only by the opportunity set and managerial motivations (Jensen and Meckling, 1976). Thus, they place primary emphasis on profitability to signal whether their return expectations will be met. Operating cash flow and solvency are secondary concerns to investors (Ettredge and Fuller, 1991). Creditors have a fixed return and are exposed to agency issues that motivate management to take risks not anticipated at the initial lending decision (Jensen and Meckling, 1976). Creditors then turn their primary focus towards solvency with profitability as a secondary concern. Hence, creditors likely place emphasis on liquidity and cash flow as signals indicating creditworthiness. Operating cash flow helps creditors identify the company's ability to generate cash flow from their ongoing business.
activities. As such, we would expect creditors to have a clear understanding regarding the relationships between changes in operating cash flow and creditworthiness.

Shinwoo (2010) has noted that generally, the financial weakness of a non-profit organization limits the quality and quantity of services that it provides to people. Especially, during the era of economic crisis, like today, a non-profit organization may be in a difficult financial condition as a result of decreasing funding from the government or donors. Thus, nowadays, it is more important for a non-profit organization to maintain strong financial condition to sustain its existing level of services. If a nonprofit organization reduces its service offerings when an external financial shock like the economic crisis occurs, the organization can be defined as financially vulnerable (Tuckman and Chang, 1991). To understand whether an organization is financially vulnerable or not, an organization should know its current financial performance. Of course, most directors and staff members of non-profit organizations usually monitor their organizations’ revenue and expenditure. However, as Siciliano (1996) empirically studied, some organizations have board members, staffs and directors who have financial management training, while other organizations have board members, staff members and directors with limited backgrounds in financial management. As a result, board members, staff and directors who have limited backgrounds in financial management have difficulty understanding and improving their organization’s financial performance.

According to Stolowy et al (2006) on the empirical study on the usefulness of disclosing both direct and indirect cash flows, they note that other studies are interested in the determinants of the comprehensiveness of cash disclosures. By using a U.K. sample, Wallace, Chodhury and Adhikari (1999) suggest that such comprehensiveness is an increasing function of firm size and the decreasing function of return on sales. They also show there are significant differences in cash flow reporting comprehensiveness among industrial groups and between positive and negative net cash flows firms.

According to Zietlow (2007) maintaining liquidity is crucial for your organization, because cash is the lifeblood of your organization’s finances. Running a donative nonprofit is especially risky, in that you are basically raising your financing from ground zero each and every year. Having
liquid resources helps you bridge the dry season and gives some breathing room when contributions resulting from your fundraising shows year-over-year declines. These resources also provide the fuel for program expansions and provisions for emergency needs such as disaster relief aid.

2.4 Financial Performance Measurement in NGOs

The comparisons of financial performance among nonprofit organizations gained popularity in the 1960s and 1970s as the method to prevent publicized fundraising abuses. Since 1990s, there have been several empirical studies that measured the financial performance of nonprofit organizations using various financial ratios (Greenlee and Bukovinsky, 1998).

Among many studies, Tuckman and Chang (1991) mentioned the unreliability of applying financial ratios derived from private sector to nonprofit organizations and developed financial ratios applicable to nonprofit organizations. They suggested four financial ratios to define whether a charitable nonprofit organization is financially vulnerable or not and applied the ratios to the sample organizations of 4,730 U.S charitable nonprofit organizations. The developed financial ratios are ‘Inadequate Equity Balances,’ ‘Revenue Concentration,’ ‘Low Administrative Costs,’ and ‘Low or Negative Operating Margins.’ Greenlee and Bukovinsky (1998) also attempted to provide key financial ratios for different types of charitable organizations. They pointed out that many traditional financial ratios are not applicable to nonprofit organizations because “charities lack the profit motive common to for-profit organizations,” and “many charities rely on voluntary contributions from individuals and corporations rather than the sale of products or services.”

Greenlee and Bukovinsky (1998), found that three ratios are useful to evaluate financial performance of non-profit organizations, and categorized those ratios as fiscal performance ratio, fundraising efficiency ratio, and public support ratio. Especially, their study supports the view of Herman and Renz (1999) that “nonprofit organizational effectiveness is multidimensional and will never be reducible to a single measure.” That is, their study shows that the financial performance of an organization cannot be simply measured by a single ratio.

First, the fiscal performance ratio shows the fiscal-management status of each organization, and this category is calculated as the ratio of total revenues to total expenses (Siciliano, 1997). Basically, all
nonprofit organizations keep their reserves like cash and bequests. These reserves are used to offset the operating deficit. Without considering reserves, the fiscal performance ratio can give an incorrect view of the fiscal performance of nonprofit organizations. Thus, in this study, the fiscal performance is calculated by the ratio of the sum of total revenue and reserves to total expenses.

Second, the fundraising efficiency ratio measures the relationship between fundraising costs and total contributions and indicates the amount of contributions raised for each dollar of fundraising cost incurred (Greenlee and Bukovinsky, 1998). This ratio is calculated as the ratio of fundraising expenses divided by total contributions. As the ratio becomes lower, it shows greater efficiency. Typical standards say that nonprofits should spend no more than 25 to 50 percent of contributions on fundraising (Hager and Flack, 2004).

Third, the public support ratio indicates the extent of an organization’s dependency on direct public support and is calculated as the ratio of total contributions divided by total revenue. Public support includes gifts, grants, and other contributions from government and donors. A ratio that is high or increasing is not desirable because the contributions are very flexible and unpredictable (Greenlee and Bukovinsky, 1998). As Denison and Beard (2003) mentioned, an organization can be more vulnerable to financial shock when revenue sources are concentrated on a specific source. There is no standard for this ratio, but usually the lower ratio means the better performance because a nonprofit organization can be less vulnerable to financial shock when revenue sources are not concentrated on only a specific source like public support.

However, as Ritchie and Kolodinsky (2003) said, there has not been enough empirical research to show the confidence in measuring financial performance of nonprofit organizations, while the importance of financial performance has been emphasized continuously. Thus, we need to consider which ratios are appropriate to measure financial performance of non-profit organizations.

2.5 Cash Flow Management in NGOs
Cash is a vital resource for a not-for-profit organization. To maintain financial viability, the organization must have enough cash to pay its bills. Accrual basis financial statements can report an excess of revenues over expenses but this does not necessarily mean that there is cash in the bank. Cyclical and seasonal fluctuations also have an impact on an organization’s cash. Cash
inflows and outflows for most not-for-profits typically fluctuate throughout the year. This increases the importance of the budgeting process because obligations must be met on a timely and consistent basis. The organization must plan ahead for those periods when cash inflow tends to be less than cash outflows. Postponing expenditures or accelerating constituent billings are two options for solving the problem (Horngren, et al, 1997)

Blazek (1996) once the annual operating and capital budgets are authorized, they can be converted into cash flow budgets to verify the availability of resources and to highlight times of lower than expected cash flow. The process includes estimating when collections on year-end receivables will occur; calculating the normal time lag between invoicing or billing for services or pledges and the actual receipt of cash; and charting the expected expenditure of cash according to the month payment is due. Then factor in the expected capital expenditures, sales of assets, borrowing, debt repayment and other financing transactions.

Cash flow statement has been studied in the past under various aspects. Some researchers are interested in the regulation aspects of cash flow statement. For example, Wallace and Collier (1991) did an international comparison on the definition of “cash”, while Stolowy and Welser-Prochazka (1992) and Wallace and Choudhury (1997) also carried out an international comparison but focused on several aspects of the cash flow statement, including the format adopted for reporting cash flow and the treatment of some specific elements (interests, dividends...). There were also several discussions on the FASB statement No. 95 on cash flow statement (Nurnberg, 1993).

Cash management has the following purposes: controlling spending in the aggregate, implementing the budget efficiently, minimizing of the cost of government borrowing, and maximizing the opportunity cost of resources (Hughes, 2007: Fabozzi & Peterson, 2003). Control of cash is a key element in macroeconomic and budget management. However, it must be complemented by an adequate system for managing commitment (Foster, 1997). It is necessary to minimize transaction costs and to borrow at the lowest interest rate or to generate additional cash by investing in revenue-yielding paper.
According to Foster (1997), during the business cycle, there will be more money flowing in than flowing out. This will allow you to build up cash balances with which to plug cash flow gaps, seek expansion and reassure lenders and investors about the health of your business. Fabozzi & Peterson, (2003) state that management of cash flows is very vital to the operations of any organization as it must remain liquid enough to be able to finance its short-term or immediate obligations. The management of cash flows must be in such a manner that the liquid cash is not in excess but must be balanced against the fixed assets. This means that the sources of finances and the application must be carefully managed (Hughes, 2007).

Academics have long advocated the importance and usefulness of the cash flow statement (Gup and Dugan, 1988; Jones, 1998; Sharma and Iselin, 2003). The cash flow statement is unique from the other financial statements because estimates and accruals are not included, making it relatively free from bias. A variety of studies support this perspective, arguing cash flow information to be as, or more useful than accrual information for decision-making (Jones, 1998).

The (total) net cash flow of a company over a period (typically a quarter or a full year) is equal to the change in cash balance over this period: positive if the cash balance increases (more cash becomes available), negative if the cash balance decreases. The total net cash flow is the sum of cash flows that are classified in three areas:

### 2.5.1 Categories of Cash Flows

In financial accounting, operating cash flow (OCF), cash flow provided by operations or cash flow from operating activities refers to the amount of cash a company generates from the revenues it brings in, excluding costs associated with long-term investment on capital items or investment in securities. The International Financial Reporting Standards defines operating cash flow as cash generated from operations less taxation and interest paid, investment income received and less dividends paid gives rise to operating cash flows. To calculate cash generated from operations, one must calculate cash generated from customers and cash paid to suppliers. The difference between the two reflects cash generated from operations. Under IAS 7, operating cash flows include: receipts from the sale of goods or services, receipts for the sale of loans, debt
or equity instruments in a trading portfolio, interest received on loans, dividends received on equity securities, payments to suppliers for goods and services, payments to employees or on behalf of employees, interest payments (alternatively, this can be reported under financing activities in IAS 7, and US GAAP).

Cash flow from investing activities refers to an item on the cash flow statement that reports the aggregate change in a company's cash position resulting from any gains (or losses) from investments in the financial markets and operating subsidiaries, and changes resulting from amounts spent on investments in capital assets such as plant and equipment. Examples of investing activities are; purchase or sale of an asset (assets can be land, building, equipment, marketable securities, etc.), loans made to suppliers or received from customers and payments related to mergers and acquisitions. When analyzing a company's cash flow statement, it is important to consider each of the various sections which contribute to the overall change in cash position. In many cases, a firm may have negative overall cash flow for a given quarter, but if the company can generate positive cash flow from its business operations, the negative overall cash flow may be a result of heavy investment expenditures, which is not necessarily a bad thing.

Cash flow from financing activities refers to a category in the cash flow statement that accounts for external activities such as issuing cash dividends, adding or changing loans, or issuing and selling more stock. This section of the statement of cash flows measures the flow of cash between a firm and its owners and creditors. Negative numbers can mean the company is servicing debt, but it can also mean the company is making dividend payments and stock repurchases, which investors might be glad to see. Financing activities include the inflow of cash from investors such as banks and shareholders, as well as the outflow of cash to shareholders as dividends as the company generates income. Other activities which impact the long-term liabilities and equity of the company are also listed in the financing activities section of the cash flow statement. Examples of financing activities include; proceeds from issuing short-term or long-term debt, payments of dividends, payments for repurchase of company shares, repayment of debt principal, including capital leases, for non-profit organizations, receipts of donor-restricted cash that is limited to long-term purposes (Investopedia.com).
2.6 Summary of the Chapter

A review of literature on the relationship of cash flow management and financial management takes a look at the theories that underpin the topic of discussion namely the accrual theory of accounting, the trade credit theory and the agency theory. The chapter then takes a review of the empirical studies that have been carried out around the area of financial performance and cash flow management of nonprofit organizations. The existing literatures reveal that there are contradicting views on the measurement criterion for financial performance of nonprofit organizations. Tuckman and Chang (1991) suggested four financial ratios to define whether a charitable nonprofit organization is financially vulnerable or not and applied the ratios to the sample organizations of 4,730 U.S charitable nonprofit organizations. Greenlee and Bukovinsky (1998), found that three ratios are useful to evaluate financial performance of non-profit organizations. Clearly, there has not been enough empirical research to show the confidence in measuring financial performance of nonprofit organizations, while the importance of financial performance has been emphasized continuously (Ritchie and Kolodinsky, 2003). Finally on the cash flow management the chapter discusses cash flow management, the cash flow statement and the total net cash flows: the cash flow from operating activities, cash flow from investing activities and cash flow from financing activities.
CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction
This chapter describes the methods that were employed to provide answers to the research objective as stated in chapter one. The following aspects of research methodology are discussed; research design, study population, research instruments, validity and reliability, data collection procedure and data analysis.

3.2 Research Design
This study adopted a causal design. This is the research conducted to identify the cause-and-effect relationship among variables when the research problem has been narrowly defined. Indeed at the heart of all scientific explanations is the idea of causality, that is, an independent variable is expected to produce a change in the dependent variable in the direction and of the magnitude specified by the theory (Frankfort-Nachmias, 1996). In practice, the demonstration of causality involves three distinct operations: demonstrating covariation, eliminating spurious relations, and establishing the time order of the occurrences.

The study aimed at collecting information on the relationship between cash flow management and financial performance of the NGOs in Kenya. Frankfort-Nachmias (1996) has recommended that in scientific research, the notion of covariation is expressed through measure of relations commonly referred to as correlations or associations. Thus in order to infer that one phenomenon causes another, a researcher must find the evidence of correlation between the phenomena. For example, if poverty is not correlated (does not vary) with violence, it cannot be the cause of violence.

3.3 Study Population
The research involved all NGOs in Nairobi. Nairobi has 2681 NGOs (NGOs Coordination Board website). In a survey conducted in the mid 1990s it was found that 755 of all registered NGOs were located in Nairobi (Mbote, 2002). Musebe (2006) found that out of 2541 registered NGOs,
1627 were located in Nairobi area forming 64% out of the population of NGOs in Kenya. The Report of NGOs Validation Survey of 2009 shows that there are 5,929 NGOs registered with the NGOs Coordination Board. Thus the population of NGOs in Nairobi was selected due to its representation of total population of NGOs in Kenya, its proximity to the researcher and the cost implications in terms of time and funds.

3.4 Sampling
A sample of 40 NGOs was systematically selected. The audited financial statements, as filed with the NGO Coordination Board, of the selected NGOs were studied and the relevant figures for the cash flows and financial performance covering five years were computed.

3.5 Data Collection Procedure
The study used secondary data. The data on the NGOs cash flows and financial performance indicator (fiscal performance were obtained from the NGOs Coordination Board data bank of filed audited financial returns by NGOs registered in Kenya covering the years of study, 2006 to 2010. The researcher analyzed the financial statements and extracted the relevant figures for computing the amounts of the various cash flows and the fiscal performance ratio used in the final analysis of the causal relationship among the variables.

3.6 Data Analysis
Using financial reports for the years 2006 to 2010, total net cash flows, cash flows from operating activities, cash flows from investing activities, cash flows from financing activities and fiscal performance ratio were calculated as averages for the five years of the NGOs.

Basic analysis begun with the determination of the various measures of central tendency namely: mean, mode, and median. The standard deviation and range were used as measures of dispersion (variation).

Both simple regression and multiple regression analysis were performed to establish the relationship between cash flows and financial performance indicator, that is, fiscal performance
ratio. Average cash flows will be regressed against the performance indicator for the same period.

The following regression model was used.

\[ Y = a + b_1 x_1 + b_2 x_2 + b_3 x_3 + \epsilon \]

Where:

- \( Y \) = the financial performance indicator (fiscal performance ratio),
- \( x_1 \) = cash flows from operating activities,
- \( x_2 \) = cash flows from investing activities,
- \( x_3 \) = cash flows from financing activities.

- \( b_1 \), \( b_2 \) and \( b_3 \) = the gradients of cash flows from operating activities, cash flows from investing activities and cash flows from financing activities respectively
- \( a \) = a constant; and
- \( \epsilon \) = the error term.

Coefficient of Correlation, (R), was used to establish the relationship between fiscal performance ratio as a dependent variable and various cash flows as independent variables. A positive R showed a direct relationship while a negative R showed an indirect/inverse relationship.

Coefficient of Determination, (\( R^2 \)) used to measure the total variation in the dependent variable (performance indicator) that was accounted for by the variation in the independent variable (cash flows). It provided a measure of how well future outcomes are likely to be predicted by the model.

F-test was used to test the significance of the overall model. The null hypothesis (i.e. the model lacking explanatory power) was rejected when the significance value F-statistic was less than 0.05 (significance level).
Durbin-Watson test used to test for autocorrelation in the model. It will test the independence of each value of the cash flows at different observations. Durbin-Watson value above 2 showed the absence of autocorrelation and a value of below 2 showed positive serial correlations.

T-test was used to test for the significance of each predictor variables (cash flows) in the model. The null hypothesis (i.e. the model lacking explanatory power) was rejected when the significance value t-statistic was less than 0.05 (significance level).
CHAPTER FOUR
DATA ANALYSIS AND PRESENTATION OF FINDINGS

4.1 Introduction
The objective of this study was to establish the relationship between cash flows management and
the financial performance of NGOs in Kenya. In order to achieve this objective, both simple and
multiple regression analysis were performed to establish the relations between cash flows and
financial performance indicator, the fiscal performance ratio, as measured by the liquidity level.
This chapter discusses the descriptive statistics of the NGOs surveyed, measures of central
tendency for the cash flows, and it also carries out and analysis correlation analysis, the
significance of predictor variables and test of overall model and autocorrelation.

4.2 Descriptive Statistics of NGOs Surveyed
Table 1: Measures of central tendency for fiscal performance ratio

<table>
<thead>
<tr>
<th></th>
<th>FPR (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>6.90</td>
</tr>
<tr>
<td>Median</td>
<td>8.00</td>
</tr>
<tr>
<td>Mode</td>
<td>6.0</td>
</tr>
<tr>
<td>Std Deviation</td>
<td>16</td>
</tr>
<tr>
<td>Range</td>
<td>116</td>
</tr>
<tr>
<td>N</td>
<td>40</td>
</tr>
</tbody>
</table>

Table 1 and 2 presents descriptive statistics for the 40 NGOs in the sample.

The average mean of fiscal performance of 40 NGOs studied was 6.90% with median as 8.0%
and standard deviation of 16%. The range was 116%.
Table 2: Measures of central tendency for cash flows.

<table>
<thead>
<tr>
<th></th>
<th>Operating Kshs. Kshs (000)</th>
<th>Investing Kshs Kshs (000)</th>
<th>Financing Kshs Kshs (000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>-104,668.00</td>
<td>60,979.00</td>
<td>-208,420.00</td>
</tr>
<tr>
<td>Median</td>
<td>-43,552.00</td>
<td>16,400.00</td>
<td>-92,620.00</td>
</tr>
<tr>
<td>Mode</td>
<td>-675,888.00</td>
<td>-191,612.00</td>
<td>-1,245,300.00</td>
</tr>
<tr>
<td>Std Deviation</td>
<td>191,630.00</td>
<td>160,318.00</td>
<td>-380,160.00</td>
</tr>
<tr>
<td>Range</td>
<td>757,542.00</td>
<td>582,034.00</td>
<td>240,731.00</td>
</tr>
<tr>
<td>N</td>
<td>40</td>
<td>40</td>
<td>40</td>
</tr>
</tbody>
</table>

The mean cash flows from operating activities was established to be Kshs. 104,668,000 compared to Kshs. 60,979,000 from investing activities and Ksh. -208,420,000 from financing activities.

The median for cash flows from operating activities, investing activities and financing activities was Kshs. -43,552,000, Kshs. 16,400,000 and Kshs. -92,620,000 respectively.

Multiple modes existed in all the categories of cash flows. In such cases the modes with the lowest values were shown. Thus the modes shown were Kshs. -675,888,000, Kshs. -191,612,000 and Kshs. -1,245,300,000 representing cash flows from operating activities, investing activities and financing activities respectively.

Deviations from mean (standard deviations) were Kshs. 191,630,000 for cash flows from operating activities, Kshs. 160,318,000 for cash flows from investing activities and Kshs. -380,160,000 for cash flows from financing activities.

There was a range of values to the tune of Kshs. 757,552,000 for cash flows from operating activities, Kshs. 582,034,000 for cash flows from investing activities and Kshs. 240,731,000 for cash flows from financing activities.
4.3 Correlation Analysis

Table 3: Pearson Correlation (R)

<table>
<thead>
<tr>
<th></th>
<th>Operating</th>
<th>Investing</th>
<th>Financing</th>
<th>Fiscal Performance Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating</td>
<td>1</td>
<td>-0.84</td>
<td>-0.88</td>
<td>0.44</td>
</tr>
<tr>
<td>Investing</td>
<td>-0.84</td>
<td>0.97</td>
<td>0.76</td>
<td>-0.38</td>
</tr>
<tr>
<td>Financing</td>
<td>-0.78</td>
<td>0.69</td>
<td>1.00</td>
<td>-0.5</td>
</tr>
</tbody>
</table>

Table 3 above represents a pearsonian correlation matrix for the various variables employed in the study.

There was a positive relationship between fiscal performance ratio and cash flows from operating activities with a correlation coefficient of 0.44 as opposed to negative /inverse relationship with both cash flows from investing activities and cash flows from financing activities whose coefficients of correlation were -0.38 and -0.5 respectively.

4.4 Test of Overall Model and Autocorrelation

Table 4: Test of overall model and autocorrelation-multiple regression.

<table>
<thead>
<tr>
<th>Dependent Variable</th>
<th>R² (%)</th>
<th>F-Test Sig. α</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fiscal Performance Ratio</td>
<td>13.60</td>
<td>0.45</td>
<td>1.80</td>
</tr>
</tbody>
</table>

N.B. All computations made using 0.05 as significance level.

Table 4 above presents the results from test of overall model and autocorrelation for multiple regression model.

When fiscal performance as a performance indicator (dependent variable) is regressed against cash flows (predictor variable) R², the coefficient of determination is 0.1360; thus 13.60% of the
total variation is accounted by the variations in cash flows. The F-significant is 0.45 while the Durbin-Watson is 1.80

Table 5: Test of overall model and autocorrelation-simple regressions

<table>
<thead>
<tr>
<th>Dependent Variable</th>
<th>Independent Variable</th>
<th>$R^2$ (%)</th>
<th>F-Test Sig.$\alpha$</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fiscal Performance Ratio</td>
<td>Operating</td>
<td>8.6</td>
<td>0.088</td>
<td>2.367</td>
</tr>
<tr>
<td></td>
<td>Investing</td>
<td>7.2</td>
<td>0.174</td>
<td>2.145</td>
</tr>
<tr>
<td></td>
<td>Financing</td>
<td>11.4</td>
<td>0.046</td>
<td>2.126</td>
</tr>
</tbody>
</table>

Table 5 presents the results from tests of overall model and autocorrelation for simple regression models.

When fiscal performance ratio is regressed against cash flows from operating activities, coefficient of determination $R^2$ is 0.086, thus 8.6% of the total variations in fiscal performance are accounted for by the variation in cash flow from operating activities. Significant F is 0.087 while Durbin-Watson is 2.367.

When fiscal performance ratio is regressed against cash flows from investing activities, coefficient of determination $R^2$ is 0.072, thus 7.2% of the total variations in fiscal performance are accounted for by the variation in cash flow from operating activities. Significant F is 0.174 while Durbin-Watson is 2.145.

When fiscal performance ratio is regressed against cash flows from financing activities, coefficient of determination $R^2$ is 0.0114, thus 11.4% of the total variations in fiscal performance ratio are accounted for by the variation in cash flow from operating activities. Significant F is 0.046 while Durbin-Watson is 2.126.
4.5 Test of Significance of Predictor Variables

Table 6. Individual parameters test-multiple regression

<table>
<thead>
<tr>
<th>Fiscal Performance Ratio</th>
<th>Cash Flow Activity</th>
<th>$\beta_1$</th>
<th>T-Test Sig $\alpha$</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Operating</td>
<td>$-1.26*10^{-8}$</td>
<td>0.94</td>
</tr>
<tr>
<td></td>
<td>Investing</td>
<td>$-1.84*10^{-8}$</td>
<td>0.899</td>
</tr>
<tr>
<td></td>
<td>Financing</td>
<td>$-1.66*10^{-7}$</td>
<td>0.62</td>
</tr>
<tr>
<td></td>
<td>Constant ($\beta_0$)</td>
<td>$4.24*10^{-2}$</td>
<td>0.121</td>
</tr>
</tbody>
</table>

N.B. Computations in table 6 made using 0.05 as significance level.

Table 6 presents the results from tests of significance of predictor variables when multiple regression model is used.

When fiscal performance ratio is regressed against cash flows using the multiple regression model, the slopes of the predictor variables are $-1.26*10^{-8}$, $-1.84*10^{-8}$ and $-1.66*10^{-7}$ for cash flows from operating activities, investing activities and financing activities respectively with a constant of $4.24*10^{-2}$. Significant t-values for cash flows from operating activities, investing activities and financing activities are 0.94, 0.899, and 0.62 respectively with 0.121 as the value for the constant.

4.6 Summary and Interpretation of Findings

There is a positive or direct association between cash-flows from operating activities and fiscal performance ratio indicator of financial performance of NGOs as evidenced by pearsonian coefficients of correlation.

There is negative or indirect association between cash flows from investing activities and cash flow from financing activities and fiscal performance ratio indicator of financial performance of NGOs as reflected by pearsonian coefficients of correlation.
Arising from the overall model and auto correlation, there is a weak relationship between cash flows management and the financial performance indicator as evidenced by the low coefficient of determination ($R^2$) and F-tests. The multiple regression model explains only 13.6% of the variations in fiscal performance ratio. The model therefore has a weak explanatory power.

From the results of the tests of auto correlation summarized on table 4, fiscal performance ratio signifies a condition of auto correlation since their Durbin-Watson values are less than two (2).

Arising from the results from tests of individual parameters as summarized on table 6, all the cash flows considered individually has minimal contribution of the overall model.

There was a positive relationship between fiscal performance ratio and cash flows from operating activities with a correlation coefficient of 0.44 as opposed to negative /inverse relationship with both cash flows from investing activities and cash flows from financing activities whose coefficients of correlation were -0.38 and -0.5 respectively.

When fiscal performance ratio is regressed against cash flows from operating activities, coefficient of determination $R^2$ is 0.086, thus 8.6% of the total variations in fiscal performance are accounted for by the variation in cash flow from operating activities. Significant F is 0.087 while Durbin-Watson is 2.367.

When fiscal performance ratio is regressed against cash flows from investing activities, coefficient of determination $R^2$ is 0.072, thus 7.2% of the total variations in fiscal performance are accounted for by the variation in cash flow from operating activities. Significant F is 0.174 while Durbin-Watson is 2.145.

When fiscal performance ratio is regressed against cash flows from financing activities, coefficient of determination $R^2$ is 0.0114, thus 11.4% of the total variations in fiscal performance ratio are accounted for by the variation in cash flow from operating activities. Significant F is 0.046 while Durbin-Watson is 2.126.
When fiscal performance ratio is regressed against cash flows using the multiple regression model, the slopes of the predictor variables are \(-1.26 \times 10^{-8}\), \(-1.84 \times 10^{-8}\) and \(-1.66 \times 10^{-7}\) for cash flows from operating activities, investing activities and financing activities respectively with a constant of \(4.24 \times 10^2\). Significant t-values for cash flows from operating activities, investing activities and financing activities are 0.94, 0.899, and 0.62 respectively with 0.121 as the value for the constant.
CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1. Summary of the Study

The study on the relationship between cash flows management and financial management of NGOs in Kenya by introducing the study and the background to the study. Chapter one also gives an overview of the financial performance of NGOs in before it states the problem of the study, its objectives and the significance of the study. Chapter two embarks on literature review, the theories underlying the study and the empirical studies of the study. It further takes a look at the cash flow management and financial performance of the non profit organizations. Chapter three explains the methodology of the study as explained by describing the research design, study population, sample, data collection and analysis.

The objective of the study as explained in chapter one was to establish the relationship between cash flows management and the financial performance of nongovernmental organisations in Kenya.

The researcher set out to establish the relationship between cash flow management and financial performance of NGOs in Kenya using Nairobi as the case study. A sample of 40 NGOs registered with the NGOs Coordination Board and whose annual income is over Kenya shillings one million were selected. The cash flows and the financial performance indicator, fiscal performance ratio, for five years were extracted. Simple and multiple regression analysis were used to establish the relationship among the variables and conclusion based on the results made.

5.2 Conclusions

This study concludes that:

There is a positive or direct association between cash-flows from operating activities and fiscal performance ratio indicator of financial performance of NGOs as evidenced by pearsonian coefficients of correlation.
There is negative or indirect association between cash flows from investing activities and cash flow from financing activities and fiscal performance ratio indicator of financial performance of NGOs as reflected by pearsonian coefficients of correlation.

Arising from the overall model and auto correlation, there is a weak relationship between cash flows management and the financial performance indicator as evidenced by the low coefficient of determination ($R^2$) and F-tests. The multiple regression model explains only 15.7% of the variations in fiscal performance ratio. The model therefore has a weak explanatory power.

From the results of the tests of auto correlation summarized on table D, fiscal performance ratio signifies a condition of auto correlation since their Durbin-Watson values are less than two (2).

Arising from the results from tests of individual parameters as summarized on table E, all the cash flows considered individually has minimal contribution of the overall model

### 5.3 Policy Recommendations

The policy makers should come up with a draft policy and framework on the accounting and financial management and measurement of financial performance by NGOs in Kenya just like there exists International Public Sector Accounting Standards for the public sector finance management.

As non-governmental organizations continue to increase in size, quantity, and impact financial management will continue to play one of the most important role in the organization to ensure that it is fully effective towards its goals and objectives of its mission. It is therefore strongly recommended that a mechanism be established of measuring whether the programmatic objectives as agreed with the donors have been met within a given period compared the financial resources expended.

The sector should come up with a policy guideline on how to measure and keep records of public support to NGOs both in kind or in cash and the corresponding costs incurred in achieving public
support or fundraising. This is crucial in encouraging contributions from individuals and will go a long way in enhancing sustainability and reducing dependence on donor funding.

Policy makers concerned with the development of educational curriculum should also incorporate topics on financial management of NGOs in the business courses offered in the earlier stages of learning. This may greatly militate against the current lack of a clear measurement of gauging the financial performance of NGOs.

5.4 Limitations of the Study

Considering the difficult to have a perfect research situation, it is a then expected that the research will have some limitations. There is need to highlight some of these limitations so that the conclusions can be understood in view of the weaknesses of the research.

Computations of financial performance indicators are based on the accounting data. Accounting policies and practices differ between NGOs and this may introduce bias into the study. Some NGOs do not file all the required financial statements for instance the statement of cash flows left out by significant number of NGOs making financial reports.

The study focused only on the NGOs registered with NGOs Coordination Board and whose annual income is in excess of Kenya shillings one million. It was assumed that all these NGOs file returns consistently. However, there are less than one hundred and twenty out of two thousand and eighty one NGOs operating in Nairobi who are consistent in filing returns for the years studied. Consequently, the findings of this study may not be generalized.

Two critical indicators of financial performance of NGOs were not applied in this study due to lack of data from the returns made by NGOs studied. These are the public support ratio and fundraising efficiency ratio. As a result only one financial performance indicator was used. Therefore to make the study results more valid all the financial performance indicators should be applied on the same study at the same time. This is more so given that a single financial performance indicator cannot be used to measure the financial performance of an organization.
5.5 Suggestions for Further Studies

Further research on cash flows management and financial performance of NGOs could focus on the following areas.

Undertake research to establish the relationship if any between NGOs size/scope, cash flows management and public support ratio and fundraising efficiency ratio as financial performance measures of NGOs.

Further research should be undertaken to establish the impact of the financial resources used by NGOs on the economic welfare of the intended beneficiaries. This will go a long way in addressing issues to do with downward accountability of NGOs towards those they purport to promote their wellbeing.

As effective financial management is a good indicator of prudent fiscal stewardship, studies should be carried out to establish the relationship between good corporate governance and financial performance of NGOs. A focused empirical research should be undertaken to show the confidence in measuring the financial performance of non-profit organizations.

As non-governmental organizations continue to increase in size, quantity, and impact financial management will continue to play one of the most important role in the organization to ensure that it is fully effective towards its goals and objectives of its mission.
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Appendix 1

Letter of Introduction

Kissing Kimonge
MBA Student, School of Business
University of Nairobi
P.O. Box 76634-00508
Nairobi-Kenya
10th October, 2011

The Executive Director
NGOs Coordination Board
P.O. Box 44617-00100
Nairobi-Kenya

Dear Sir,

RE: Collection of Research Data for MBA Project.
I am a post graduate student at the University of Nairobi, School of Business. In order to fulfill the degree requirements I am undertaking a research project on “Relationship between cash flow management and financial performance of NGOs in Kenya; Case of Nairobi Area” as part of the academic requirements towards completion of the course.

Your organization has been selected as part of this study. This is to kindly request you to assist me to collect the data by providing access to selected data within your organization. I need access to the audited financial reports by of a sample of 60 NGOs operating in Nairobi covering the period 2005-2010. Specifically I need information on the Statement of Cash Flows and Income and Expenditure Statement. I am aware that I search fees of Kshs. 2,000 per a search is applicable. However, since the information I need is purely for academic purposes and that I do
not have preference for any particular NGO's financial information I request that the whole exercise be considered as one search.

The information that you are going to provide will be used exclusively for academic purposes and will be treated with strict confidence. At no time will your name appear in the report. Appropriate acknowledgements will be given to you and your organization with your prior permission. A copy of the final paper will be availed to you upon request.

Your cooperation will be highly appreciated.

Thank you in advance.

Yours faithfully,

Kissinger Kimonge
MBA Student
School of Business
University of Nairobi
Appendix 2

List of NGOs Surveyed in the Study

1. THE BRITISH INSTITUTE IN EASTERN AFRICA
2. MAJI NA UFANISI WATER AND DEVELOPMENT
3. MUSIC FOR LIFE
4. AVSI FOUNDATION
5. FARMING SYSTEMS
6. COMMUNITY AID INTERNATIONAL
7. AFRICA HEALTH AND DEVELOPMENT INTERNATIONAL
8. AFRICAN WOMEN'S DEVELOPMENT AND COMMUNICATION NETWORK
9. CENTRE FOR PEACE AND DEMOCRACY
10. CHOSEN CHILDREN OF PROMISE

11. COMMUNITY VISIONS (LIAISON, EDUCATION AND ACTION FOR DEVELOPMENT)
12. COOPT-COOPERAZIONE INTERNAZIONALE
13. CROSS CURRENT INDIGENEOUS NETWORK
14. DORCAS AID INTERNATIONAL - AFRICA
15. ECUMENICAL PHARMACEUTICAL NETWORK
16. EQUALITY NOW
17. FARMING SYSTEMS KENYA
18. GETHSEMANE INTERNATIONAL - AFRICA, INC
19. GOOD PEOPLE WORLD FAMILY
20. HELPAGE KENYA
21. HORN RELIEF
22. INTERNATIONAL BIBLE SOCIETY EAST AFRICA
23. INTERNATIONAL REPUBLICAN INSTITUTE
24. KENYA CHRISTIAN INDUSTRIAL TRAINING INSTITUTE (KCITI)
25. KENYA WOMEN FINANCE TRUST
26. LIFE IN ABUNDANCE- KENYA
27. MAPENDO INTERNATIONAL
28. MAZINGIRA INSTITUTE
29. MISSION OF HOPE INTERNATIONAL
30. MUSIC FOR LIFE KENYA
31. NAIROBI HOSPICE (NAIROBI TERMINAL CARE CENTRE)
32. NAZARENE COMPASSIONATE ORGANIZATION
33. ORGANIZATION FOR ASSISTING HEARING IMPAIRED PERSONS
34. PACT KENYA
35. PRACTICAL ACTION
36 RELIEF FOUNDATION
37 SOLAR COOKERS INTERNATIONAL (E.A)
38 SUMMER INSTITUTE OF LINGUISTICS
39 TAKE HEART ASSOCIATION PROJECT
40 THE PALMHOUSE FOUNDATION
TO WHOM IT MAY CONCERN

The bearer of this letter, Kisicinger Henry Kimonge, Registration No. D61/70981/2007, is a bona fide continuing student in the Master of Business Administration (MBA) degree program in this University.

He/she is required to submit as part of his/her coursework assessment a research project report on a management problem. We would like the students to do their projects on problems affecting firms in Kenya. We would, therefore, appreciate your assistance in enabling him/her to collect data in your organization.

The results of the report will be used solely for academic purposes and a copy of the same will be availed to the interviewed organizations on request.

Thank you.

JUSTINE MAGUTU
ASSISTANT REGISTRAR
MBA OFFICE, AMBANK HOUSE
MBA Research Data

To: Douglas Owino

Subject: MBA Research Data

Dear Douglas,

This is my e-mail address you can use to reach me for any progress on my request for access to financial information on NGOs. I really appreciate your kind support this far.

Have a blessed evening.

Thanks,

Kissinger Kimonge