

**THE EFFECT OF EXCHANGE RATE VOLATILITY ON BUDGET VARIANCE
OF INTERNATIONAL REFUGEE NON GOVERNMENTAL ORGANIZATIONS
IN KENYA**

BY

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DECLARATION

This research project Proposal is my original work and has not been presented for award of any degree in any university.

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DEDICATION

I dedicate this work to my son Ryan Gimona. A special dedication to my loving wife Mrs. Lillian for her constant encouragement and patience during the period i was constrained of time. My parents too for their encouragement and resources they have invested in me.

TABLE OF CONTENT

DECLARATION	ii
ACKNOWLEDGEMENTS	iii
DEDICATION	iv
LIST OF TABLES	vii
LIST OF ABBREVIATIONS	viii
ABSTRACT	ix
CHAPTER ONE	1
INTRODUCTION	1
1.1 Background of the Study	1
1.1.1 Exchange Rate Volatility.....	2
1.1.2 Budget Variance	4
1.1.3 The Effect of Exchange Rate Volatility on Budget Variance.....	5
1.1.4 Refugee Non-Governmental Organization in Kenya	6
1.2 Research problem.....	8
1.3 Objectives of the study	10
1.4 Value of the study	10
CHAPTER TWO	11
LITERATURE REVIEW	11
2.1 Introduction	11
2.2 Theoretical Review	11
2.2.1 The Monetary Approach Theory.....	11
2.2.3 The Portfolio Balance Theory.....	12
2.2.4 The Purchasing Power Theory.....	12
2.2.4 The Balance of Payments Theory	13
2.3 Determinants of Budget Variance.....	14
2.3.1 Exchange Rate Volatility.....	14
2.3.2 The Nature and Utilization of Donor Funds	16
2.3.3 Partnerships	17
2.4 Empirical Review.....	19
2.5 Summary of the Literature Review	23
CHAPTER THREE	24
RESEARCH METHODOLOGY	24

3.1 Introduction	24
3.2 Research design	24
3.3 Population.....	24
3.4 Sample Size	24
3.5 Data Collection	24
3.5.1 Data Validity and Reliability	25
3.6 Data Analysis.....	25
3.6.1 Analytical Model	25
3.6.2 Test of significance	26
CHAPTER FOUR.....	27
DATA ANALYSIS, RESULTS AND DISCUSSION.....	27
4.1 Introduction	27
4.2 Descriptive statistics.....	27
4.3 Regression model, analysis and results	30
4.4 Summary and Interpretation of findings.....	32
CHAPTER FIVE	37
SUMMARY, CONCLUSIONS AND RECOMMENDATIONS	37
5.1 Introduction	37
5.2 Summary	37
5.3 Conclusion.....	38
5.4 Policy Recommendations	39
5.4 Limitations of the study.....	40
5.6 Suggestions for further Studies.....	40
REFERENCES.....	42
APPENDICES	48
Appendix I: Letter of Introduction.....	48
Appendix II: Questionnaire	49
Appendix III: Central Bank of Kenya US Dollar rates	50
Appendix IV: List of International Refugee NGO in Kenya at the NGO Coordination Board as at 31st December 2013	51

LIST OF TABLES

Table 1: Budget variance experienced by International Refuge NGOs.....	28
Table 2: Annual data summary of the Monthly Exchange Rate.....	28
Table 3: Exchange rate volatility summary for the four years.....	29
Table 4: The amount of annual budget funded in foreign currency contracts.....	29
Table 5: The amount of budget deviation experienced by Partners organization.....	29
Table 6: Linear regression model summary.....	30
Table 7: ANOVA.....	30
Table 8: Regression coefficients with Budget variance as the response variable.....	31
Table 9: Correlations.....	32

LIST OF ABBREVIATIONS

ANOVA	Analysis of Variance
BOP	Balance of Payments
CBK	Central Bank of Kenya
DAC	Development Assistance Committee
DRC	Danish Refugee Council
GARCH	Generalized Autoregressive Condition of Heteroscedasticity
IMF	International Monetary Fund
IRIN	International Regional Information Network
IRO	International Refugee Organization
KNBS	Kenya National Bureau of Statistics
MDGs	Millennium Development Goals
NGO	Non-Governmental Organization
OECD	Organization for Economic Co-operation and Development
OMB	Office of Management and Budgets
PPP	Purchasing Power Parity
RER	Real Exchange Rate
SPSS	Statistical Package for Social Science
USAID	United States Agency for International Development
US	United States

ABSTRACT

Most of the International Non-Governmental organizations in Kenya receive a significant portion of the budget funding in foreign currency contract. While the daily and monthly exchange rate in Kenya keeps on fluctuating each donor and organization has strict, different rules and technique in regard to the management of exchange rate gain or losses in the operation of its funds.

The objective of this study was to establish the effect of exchange rate volatility on budget variance of international Refugee Non-Governmental Organizations in Kenya. A descriptive study was used with secondary data collected from the different Audited Financial statement of Refugee Non-Governmental Organization and part of the data relating to partner organization which was not available in the financial statement was obtained through questionnaire as primary data for this study. The exchange rate data was obtained from the Central Bank of Kenya website. The data was analyzed using a multiple regression model to obtain the coefficients of the variables. SPSS was used to analyze the data.

Findings of the study indicated that exchange rates do indeed have a positive correlation to the budget variance. It is also noted in the findings that it was not the only factor affecting budget variance hence the study concluded that exchange rates has an effect on the budget variance besides the amount of funding in foreign currency contracts and amount of deviation in the budgets of partner organizations among other factors which were beyond the scope of this study.

The study recommends policy formulation and implementation to control and ensure a reduction in the impact of exchange rates on the organization budget variance by the international organizations. The Government should formulate policy to improve on information dissemination to reduce exchange rate risk and allow for relative estimation and prediction of exchange rate to foster proper financial planning.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Exchange rate risk management is an integral part of every firm's decisions about foreign currency exposure (Allayannis, Ihrig, and Weston, 2001). Exchange rate is a function of international financial relative price. The International Refugee non-governmental organization does not have any control on the prevailing exchange rates, despite the dollar rates accounting to substantial amount of transactions and grants received. In Kenya, the subject has been at the center of economic policy debate, involving policymakers, the business community, academic researchers, and the business press. All point out the potential deleterious effects of "excessive" volatility observed in the country's currency market since the adoption of a floating exchange rate in 1993 on the country's economic growth (CBK, 2002). The exchange rate variation is a major challenge experienced by Refugee non-governmental organization in three stages of budget, namely budget setting, implementation and reporting to the funders. It leads to mismatch in the income received, the actual expenditure incurred against the set budget hence the Refugee non-governmental organization are not able to efficiently break even in their performance.

Currency risk hedging strategies entail eliminating or reducing this risk, and require understanding of both the ways that the exchange rate risk could affect the operations of economic agents and techniques to deal with the consequent risk implications (Barton, Shenkir, and Walker, 2002). Selecting the appropriate hedging strategy is often a daunting task due to the complexities involved in measuring accurately current risk exposure and deciding on the appropriate degree of risk exposure that ought to be covered. The need for currency risk management started to arise after the breakdown of the Bretton Woods system and the end of the US dollar peg to gold in 1973 (Papaioannou, 2001).

During the era of the fixed exchange rate regime, that covered the period of 1966-92, Kenya, like many developing countries, had to frequently devalue its currency in an attempt to reduce the negative effects that RER volatility had on its economy. The adoption of a floating exchange rate system in 1993 marked the climax of efforts to make the RER more aligned to

the market determined equilibrium RER, and thus eliminate RER volatility. There is, however, no available evidence that success has since been achieved in realizing the objective for which the foreign exchange market was liberalized. Large volatilities in nominal exchange rates have since characterized Kenya financial market (Kiptoo 2007).

1.1.1 Exchange Rate Volatility

Exchange rate is the price of one currency quoted in terms of another currency. It is also regarded as the value of one country's currency in terms of another currency. A common definition of exchange rate risk relates to the effect of unexpected exchange rate changes on the value of the firm (Madura, 1989). In particular, it is defined as the possible direct loss (as a result of an unhedged exposure) or indirect loss in the firm's cash flows, assets and liabilities, net profit and, in turn, its stock market value from an exchange rate move.

Foreign exchange risk is the risk that the domestic currency value of cash flows dominated in foreign currency may vary because of variations in the foreign exchange rate. Currencies of many countries are not quoted against each other. Cross rate is an exchange rate between two currencies that are not quoted against each other but are quoted against one common currency. Most currencies are quoted against the United States US Dollar (Pandey, 2005).

Exchange rates of Kenya shilling to the US Dollar have undergone three major regimes from 1967 to 2009. This has been described by the fixed exchange rate error, the crawling peg error and the floating/flexible error.

The Fixed exchange rate error regime was adopted at the independence to early eighties. Kenya, like many developing countries, had to frequently devalue its currency in an attempt to reduce the negative effects that RER misalignment had on its economy. The value of shillings was fixed by CBK at a certain rate of the dollar and was dominated by macro-economic management control. Fixed rate occurs when the government establishes the price of currency and maintains it through active intervention (Bryns and Stone 1987).

The Crawling peg error regime occurred between eighties and 1993 it marked the climax of efforts to make the RER more aligned to the market determined equilibrium RER, and thus eliminate RER misalignment .In the short term currencies are fixed or pegged against each

other and does not change in value whilst in the longer term, the value of the currency can be changed if economic circumstances so dictates (Anderton 2000). Under the crawling system, a country fixes its currency value against another within a band. A mechanism is built into the system which allows the band to rise and fall regularly over time. The Value of shillings was based on the availability of foreign exchange reserve at the central bank.

The floating/ flexible exchange rate regime started from 1993, Kenya adopted flexible rate system which according to (Bryns and Stone 1987) is one that is allowed to change in response to changing demand and supply conditions. The central bank does not directly set the exchange rate. If government or central bank withdraws completely from the exchange rate markets, the floats are clean, A float is dirty if central bank intervenes in exchange markets of buying or selling foreign currencies in order to affect the exchange rate (Wonnacott et al 1987). However, there is no available evidence that success has since been achieved in realizing the objective for which the foreign exchange market was liberalized.

The real exchange rate (RER), defined as the rate at which goods, and services produced at home can be exchanged for those produced in another country or group of countries abroad. It can be expressed in nominal or real terms. It is referred to as the nominal exchange rate (NER) when inflation effects are embodied in the rate, and as the (RER) when inflation influences have been excluded (Copeland, 1989:4, Lothian, and Taylor, 1997). Increased RER volatility would, for instance, increase the uncertainty of profits on contracts denominated in a foreign currency, and would therefore reduce economic growth to levels lower than would otherwise exist if uncertainty were removed (Cote, 1994).

RER volatility refers to short-term fluctuations of the RER about their longer-term trends (Frenkel and Goldstein, 1989). It also entails short-term (monthly, weekly, or even hourly) fluctuations in the exchange rates as measured by, their absolute percentage changes during a particular period (Williamson, 1985).

Various studies, particularly, in the developed and middle-income countries, have also explored the impact of exchange rate volatility and associated uncertainty on trade, investment, and economic growth. Majority of these studies have found that exchange rate volatility can affect trade directly, through uncertainty and adjustment costs, and indirectly

through its effect on the structure of output and investment (Cote, 1994, Serven, 2002, Pickard, 2003, Cheong, 2004, Kikuchi 2004, Arize et al.,2004).

1.1.2 Budget Variance

The budget is a standard against which the actual performance can be compared and measured. Budgets are used to communicate top management's expectations to managers and employees. The budgeting process provides for coordinated planning among different functional areas (Bremser, 1988). Budgets are financial blueprints that quantify a firm's plans for a future period. Budgets require the management to specify expected sales, cash inflows and outflows, and costs; and they provide a mechanism for effective planning and control in organizations (Flamholtz, 1983).

Budget deficit occurs when expenses do not match the incomes i.e. Expenditure exceeds income received. 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 management. 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. 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. The staff must be able to demonstrate that the dollars were used as directed by the donor. The shift to an emphasis in external financial reports on donor restriction has made the use of fund accounting systems even more critical. Herbert, et al, (1987), suggests that financial management control, among others, considers the following aspects, a systematic effort to set performance standards consistent with planning objectives, to design information feedback system, to compare actual performance with the predetermined standards and to take any action required to ensure that all institution or

corporate resources are used in the most effective and efficient way possible in achieving institutional objective. The financial management requirement for contracts and grants are based on a combination of awarding entities policies and those of the receiving nonprofit organizations.

Budgeting and cash management are two areas of financial management that are extremely important exercises for not-for-profit organizations. Budgets have multiple roles. (Burchell et al, 1980) say that budgets can have an "interactive" role where they are used as a "dialogue, learning and idea creation machine (p. 191)." Budgets also have a "diagnostic" role, which refers to the traditional purposes of performance management and responsibility accounting. Budgeting therefore becomes a critical activity for a not-for-profit. There is an economic argument, based on the concept of Efficiency, which argues that NGO's provide services more cost-effectively than Government agencies can and that NGO's are able to generate self-reliant and sustainable interventions. Smith (1987) found that NGO were generally more efficient to government project based on the greater costs advantage due to lower labor costs and incomplete pricing.

1.1.3 The Effect of Exchange Rate Volatility on Budget Variance

Firms have different practices in setting budget exchange rates (Lam, 2003). Many corporate treasurers of multinational firms prefer to use PPP rates as budget. Alternatively, a firm may decide to set its budget exchange rate at the daily average exchange rate over the previous fiscal year (Barton, Shenkir, and Walker, 2002). Budget exchange rates provide firms with a reference exchange rate level (Madura, 1989). Setting budget exchange rates is often linked to the firm's sensitivities and benchmarking priorities.

NGO need to break-even in their budget performance for the expenditure to equal the income in a given budget. The variation of exchange rates experienced during transactions against the budgeted exchange rates lead to either shortage of funds where dollar rates declines and excess of funds where a dollar rate appreciates. The amount of funds not utilized is refunded to the donor at the end of the contract agreement and if over spent, the donor does not absorb the extra costs exceeding the actual budget as approved in the agreement. In the extreme,

high spending practices may resort to crisis management, giving rise to a wide range of potentially adverse consequences.

Therefore the international Refugee NGO need to ensure it break-even in their performance for the expenditure to equal the income in a given budget and still achieve the program objectives in the most efficient manner within the available funds. However this has been complicated by the effect of the Exchange rate variations among other variables including but not limited to Donor rules and regulations requirements and implementation through Partner organizations.

1.1.4 Refugee Non-Governmental Organization in Kenya

The 1951 United Nations Convention Relating to the Status of Refugees has adopted the following definition of a refugee (in Article 1.A.2): Any person who: owing to a well-founded fear of being persecuted for reasons of race, religion, nationality, membership of a particular social group, or political opinion, is outside the country of his nationality, and is unable to or, owing to such fear, is unwilling to avail himself of the protection of that country. The concept of a refugee was expanded by the Convention's 1967 Protocol and by regional conventions in Africa and Latin America to include persons who had fled war or other violence in their home country. Different NGO has arisen to protect the plight of refugee. The examples of refugee NGOs are the Danish Refugee Council (DRC) founded in 1956 after the Second World War, and in response to the European refugee crises caused by the Soviet invasion of Hungary in 1956. The International Refugee Organization (IRO) founded on April 20, 1946 to deal with the massive refugee problem created by World War II

Non-Government Organizations (NGO,s) can be defined as private organizations “characterized primarily by humanitarian or cooperative rather than commercial objectives that pursue activities to relieve suffering, promote the interests of the poor, protect the environment, provide basic services, or undertake community development” in developing countries. (World Bank operational directive 14.70). It is a designation given to describe a group of organizations that are allowed to make profit but they are prohibited from distributing their profits or earnings to those in control of the organization. (Internal revenue service code 501 (c) (3) of the United States)

NGOs are subset of the broader nonprofit sector that engage specifically in international development and by definition non-profit entity is not to earn a profit their objectives is to render as much suitable services as needed. From this perspective NGOs are frequently idealized as organizations committed to “doing good” while setting aside profit or politics (Zivetz, 1991; Fisher, 1993). Ideally their performance is to break even. This means that by and large and on a short term basis, their income should equal costs.

Some NGOs are seen as organizations components of social movements which seek connections with institutionalized system of decision making (Mc Cathy and Zaid 1997; Dechalert 1999) .The NGOs are one group of players who are active in the efforts of international development and increasing the welfare of poor people in poor countries. They work both independently and alongside bilateral aid agencies from developed countries, private sector infrastructure operators, self – help associations and local governments. There has also been a rising involvement of non-governmental organizations (NGOs) in the development process (Edwards & Hulme 1995, Hulme & Edwards 1997). This phenomenon is partly a consequence of dissatisfaction with government performance in the delivery of public services.

The number of international NGOs rose from less than 200 in 1909 to nearly 1000 in 1956 to over 20,000(Union of International Association, 2005).The amount of the discretionally funding that high income countries have given to NGOs to promote international development assistance has risen from a negligible amount before 1980 to nearly \$2billion in 2004 (OECD, 2006a). This amount though substantial does not include additional billions of dollars that are channeled through NGOs to implement specific projects on behalf of the donor countries. One early estimate calculated the total resources disbursed for development projects through NGOs to have risen from \$ 0.9 billion to \$ 6.3 billion in 1993, measured in 1970 dollars (Riddle and Robinson, 1995).

Indeed to ignore NGOs, is to misread the history of the twentieth century world (Iriye, 1999 P424) .Development oriented NGO are not new, but have existed for centuries. For example groups that today would be labeled as NGOs helped organize the opposition that led Britain to abolish the slave trade in 1807, at which point these groups broadened their missions and

worked to ameliorate the plight of slaves and abolish slavery elsewhere (Keck and Sikkink,1998

1.2 Research problem

Most of the international Refugee Non-Governmental organizations in Kenya receive their funding and income through contracts denominate by foreign currency but transacts majority of the expenditure in Kenya shillings while they are expected to report on their budget performance in the foreign contract currency. The monthly exchange rate in Kenya keeps on fluctuating while each donor has inflexible, different policy and procedure in regard to the management of exchange rate gain or losses in the implementation of its funds.

The Exchange rate variations results from positive and negative movements in the value of a country's currency relative to a foreign currency within a given period. The country currency tends to loose or gain value against other foreign currencies. An increase in the fluctuation of the exchange rate between currencies is often the result of major changes that are occurring within the global economy and in other instances changes are direct result of fiscal and/or monetary policies undertaken by the national government of a country. These changes affects cross border trade, Global financial crises has been shown as having an impact on the exchange rate Volatility (Olowe 2011).

Excess RER volatility has been known to reduce the level of economic growth by creating uncertainty about the profits, unemployment, and poverty. It is also known to restrict the international flow of capital by reducing both direct investment in foreign operating facilities, and financial portfolio investment. Finally, increased RER volatility may lead to higher prices of internationally traded goods by causing traders to add a risk premium to cover unanticipated exchange rate fluctuations (McKinnon, and Ohno, 1997).

To manage the exchange rate risk inherent in every multinational firm's operations, a firm needs to determine the specific type of current risk exposure, the hedging strategy and the available instruments to deal with these currency risks. Multinational firms are participants in currency markets by virtue of their international transactions. To measure the impact of exchange rate movements on a firm that is involved in foreign-currency denominated operations, i.e. the implied value-at- risk (VaR) from exchange rate moves, we need to

identify the type of risks that the firm is exposed to and the amount of risk encountered (Hakala and Wystup, 2002). For their currency risk management decisions, firms with significant exchange rate exposure often need to establish an operational framework of best practices (Allen,2003; Jacque, 1996).

In spite of the abundant literature on the effects of exchange rate volatility on macroeconomic variables such as economic growth, studies that specifically focus on Kenyan economy are scanty. A related study by Ndung'u (1999) assessed whether the exchange rates in Kenya were affected by monetary policy, and whether these effects were permanent or transitory .Were et. al. (2001), analyzed factors that have influenced the exchange rate movements since the foreign exchange market was liberalized in 1993. The study by Kiptoo (2007) focused on the real exchange rate, misalignment, and its impact on the Kenya's international trade, and investment. Sifunjo (2011) investigated chaos and nonlinear dynamical approaches to predicting exchange rates in Kenya. James (2013) carried a study on the Impact of Exchange rate on diaspora remittance in Kenya. Ouma (2013) examined the impact of Central Bank Intervention on Foreign Exchange rate volatility in Kenya

The previous studies have always have laid a lot of emphasis on the budget, budgeting process, importance and implementation of budgets. In Kenya, empirical studies have been carried; Murrison (2001) carried out a survey of budgeting practices among the major British non- governmental organizations in Kenya and the extent to which budgets are used as tool of management control. Ndiritu (2007) carried a case study on the effectiveness of cash budgeting at Telkom Kenya. Muthinji (2009) did a case study on the challenges of budget implementation at Commission of Higher Education

Research gap is that so far studies done do not focus on the effect of exchange rate volatility on budget variance of international Refugee Non-governmental organizations in Kenya. Therefore this study seeks to address the research question: what is the effect of exchange rate variation on budget variance of international Refugee Non-governmental organizations in Kenya?

1.3 Objectives of the study

To establish the effect of exchange rate volatility on budget variance of International Refugee Non-Governmental Organizations in Kenya.

1.4 Value of the study

This study will therefore contribute to existing literature by examining the effect of exchange rate volatility on budget variance of international Refugee Non-Governmental Organizations in Kenya and will assist them to understand the organization's environment of operation, their relationship and relative importance in both control and decision making that in addition can enhance policy development.

The study will also offer sacrificial benefit in that it will provide a different perspective upon which further studies on budgets can be explored by academicians and researchers to add to the body of knowledge in the Finance discipline. It will also be useful to researchers as a secondary data to review their literature.

Findings and understanding of the the effect of exchange rate volatility on budget variance will benefit the international Refugee Non-Governmental Organizations in Kenya and other institutions because it will provide them with knowledge and understanding of how the exchange rate volatility affects the budget of which they receive substantial amount in foreign currency funding. The study will also contribute to theory by providing more insight into ways in which different international Refugee Non-Governmental Organizations manages the exchange rate volatilities despite the dynamic environment of operation where they do not have any control to factors that cause exchange rate volatilities. It will identify areas that need further study and will be used by students and researchers to come up with more theory on the subject of exchange rate variations and budget variance.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews various literatures that are relevant to exchange rate variation and budget variance of international Refugee NGOs in Kenya. It also presents the relevant theories that explain the exchange rate determination and budget deficit as well as empirical reviews conducted on both exchange rate and budget deficit.

2.2 Theoretical Review

Economists and financial experts are yet to agree on a single theory that defines the exchange rate.

2.2.1 The Monetary Approach Theory

Krueger (1983), the approach originated from the work of a group of economists, primarily teaching at or trained at the University of Chicago led by Mondell and Jonhson. That work had been preceded by the work of Polak and others at the IMF in the late 1950s and early 1960s. Praise (1961) and Kemp (1962) had earlier provided models capturing the essentials features of the monetary stocks flow adjustments process that were surprisingly neglected by the profession.

In this approach attention is given to the stock of currencies in comparison to the willingness of people to hold these stocks. According to the monetary theory, exchange rates adjust to ensure that the quantity of money in each currency supplied is equal to the quantity demanded (Parkin M. & King D. 1992). Both Quantity Theory of Money and Purchasing Power Parity have been used in support of the above theory. The Quantity Theory of Money states that there is a direct relationship between the quantity of money and the level of prices of goods and services sold (Investopedia.com). In other words, more money equals more inflation. An increase in the money supply leads to inflation, which in turn results in the decrease in the value of money or purchasing power. Consequently, a rapid increase in the money supply (in the home currency), which means inflation, will put into effect the

Purchasing Power Parity resulting in the depreciation of the currency's exchange rate. A higher interest rate will also result in the currency's depreciation because of the positive relationship between interest rates and money circulation.

2.2.3 The Portfolio Balance Theory

The portfolio balance approach is largely attributed to Branson (1972, 1976), Mackinnon (1969), and Dornbusch (1975), with follow ups of Branson et al (1977, 1979), Girton and Henderson (1977) and Branson and Henderson (1985). It takes into consideration the diversification of investors' portfolio assets. Diversification is a technique that attempts to reduce risk by investing both among various financial instruments and across national borders. Example, a combination of domestic and foreign money and domestic and foreign bonds. What the theory argues is that an increase in the money supply will lead to a depreciation of the exchange rate. The extent of the depreciation depends upon the fluctuation in domestic interest rates and the exchange rates. If we consider an increase in the domestic money supply, we will anticipate that a lower interest rate and /or a higher exchange rate can only absorb the excess supply, which in turn will result in the reduction of bonds.

2.2.4 The Purchasing Power Theory

The idea of Purchasing Power Theory (PPP) originated with the School of Salamanca in the 16th century and was developed in its modern form by Gustav Cassel (1918). The concept is based on the law of one price, where in the absence of transaction costs and official trade barriers, identical goods will have the same price in different markets when the prices are expressed in the same currency. The PPP theory has a long history in economics, dating back several centuries, but the specific terminology of purchasing power parity was introduced in the years after World War I during the international policy debate concerning the appropriate level for nominal exchange rates among the major industrialized countries after the large-scale inflations during and after the war (Cassel, 1918). Since then, the idea of PPP has become embedded in how many international economists think about the world. For example, Dornbusch and Krugman (1976) noted: "Under the skin of any international

economist lies a deep-seated belief in some variant of the PPP theory of the exchange rate.” Rogoff (1996) expressed much the same sentiment.

The PPP happens to be one of the most significant approaches to determine exchange rate. It is a flow model of the balance of payment. This approach lays down the fact the exchange rate has to compensate for the difference in inflation rate .The theory is based on the ‘law of one price’, which argues that should a currency price (Euro) of a good be multiplied by the exchange rate (€ /US\$) then it will result in an equal price of the good in US dollars. However, it is finally the market that through supply and demand will force accordingly the euro and US dollar prices to the equilibrium point. Thus, the law of one price will be reinstated, as well as the purchase power parity between the euro and US dollar. Inflation differentials between countries will also be eliminated in terms of their effect on the prices of the goods because the PPP will adjust to equal the ratio of their price levels¹². More specifically, as stated in their book (Lumby S. & Jones C, 1999) “the currency of the country with the higher rate of inflation will depreciate against the other country’s currency by approximately the inflation differential”.

The theory, although it describes in a sufficient way the determination of the exchange rates, is not of good value, mainly because of the following two disadvantages. Firstly, not all goods are traded internationally (for example, buildings) and secondly, the transportation cost should represent a small amount of the good’s worth. PPP is not a very reliable determinant since changes in technology, commercial policies, labor force and tastes change the national productivity, which in turn changes the real exchange rate. In accordance with the PPP concept, the inflation differentials between countries affect the exchange rate, and consequently the PPP could be of good value in order to forecast the exchange rate (Cochran & Defina, 1995).

2.2.4 The Balance of Payments Theory

The Marshall Lerner Condition is the heart of the elasticities approach to the Balance of Payment (BOP) theory, also called the (Marshall-Lerner-Robinson Condition), Marshall (1842-9124), Lerner (1903-82) and Robinson (1903-83). As it is known from macroeconomics, the balance of payments is a method of recording all the international

monetary transactions of a country during a specific period of time. The transactions recorded are divided into three categories: the current account transactions, the capital account transactions, and the central bank transactions. The aforementioned categories can show a deficit or a surplus, but theoretically the overall payments (the BOP as a whole) should be zero which rarely happens. As stated earlier, a currency's price depreciation or appreciation (the change in the value of money), directly affects the volume of a country's imports and exports and, consequently, a likely fluctuation in the exchange rates can add to BOP discrepancies. For example, a likely depreciation will increase the value of exports in home currency terms (the larger the exports demand elasticity the greater the increase). Conversely, the imports will become 'more expensive' and their value will be reduced in home currency (the larger the imports demand elasticity the greater the decrease). Unless the value of exports increases less than the value of imports, the depreciation will improve the current account. The Marshall Lerner Condition shows that if the sum of the price elasticity of demand for imports and exports is greater than one, then a fall in the exchange rate will improve the current account of BOP.

2.3 Determinants of Budget Variance

2.3.1 Exchange Rate Volatility

The impact of exchange rate movement to the international Refugee Non-Governmental organizations affects the cash flow, cost of project implementation and reporting since they are not profit making organizations. In order to minimize the possibility of financial loss, it is therefore essential that corporations with foreign exchange exposures identify measure and manage their risk effectively (Jacque, 1981).

Managing foreign exchange risk is a fundamental component in the safe and sound management of all firms or institutions that have exposures in foreign currencies. It involves prudently managing foreign currency positions in order to control, within set parameters, the impact of exchange rate on the financial positions of the institution (Adler and Duma, 1984). It is a unique complication of financial management that exposes the organization to risk in three different areas of operation.

Transaction or Contractual risk. It is basically cash flow risk and deals with the effect of exchange rate movement on transactional account exposure related to receivables (export contracts), payables (import contracts) or repatriation of dividends. The risk that the local currency value of foreign currency receipts will fall or that the local value of foreign currency payments will rise between the fixing of a contract and the date of payment or receipt. An exchange rate change in the currency of denomination of any such contract will result in a direct transaction exchange rate risk to the firm. Transaction exposure exists when the future cash transactions of a firm or individual are affected by exchange rate fluctuations. It arises out of transactions exposures which entails gains and losses that arise from settlements of transactions whose terms are stated in foreign currency (Eiteman and Stonehill, 1979).

Translation or Accounting risk. The concept of accounting exposures arises from the need to translate accounts that are denominated in foreign currencies into the home currency of the reporting entity in accordance with appropriate accounting principles. The translation risk is a multinational company's concern and its consideration may be absolutely irrelevant to many locally incorporated companies (Allayannis and Ofek, 1997). It considers the sensitivity of company value to fluctuations in foreign exchange rate. Its arises where a firm has foreign affiliates and keeping books in the respective local currency but for the purpose of reporting and consolidating the accounts it must translate its accounts to the donor contact currency or parent organization currency.

Economic risk. It represents any impact of exchange rate fluctuations on the firm's future cash flows. It is the possibility that the parent currency denominated net present value of cash flows will adversely be affected by exchange rate movements (Walker, 1978). Unlike the transaction exposure, economic exposure is long term in approach and does not only focus on hedging their currency payables or receivables but also determines how all the cash flows of a firm will be affected by possible exchange rate movement (Miller and Reuer, 1998). Economic exposure management should aim at neutralizing the impact of unexpected exchange rates changes on net cash flows between the cost and revenue side (Jacque, 1981). An Operational approach for implementing this concept of economic management was developed by Nauman- Etienne (1977). He identified managerial policies , operational

characteristics and environmental parameters to which economic exposures is sensitive ; defined protective steps to minimize adverse effects on unexpected exchange rate changes on future cash flows.

2.3.2 The Nature and Utilization of Donor Funds

The financial management of not for profit organizations are generally dominated by conditions of resource scarcity. Such organizations have limited opportunities for generating additional income, but are faced with ever increasing agenda of programme and activities of which funds could be spent (Drucker, 2000).

Donor funding concept involves giving out funds for projects by a donor agency or organization. Various principles are set in guiding management of donor funding as a result of funding gap and disconnect. The disconnect between humanitarian assistance and development cooperation does not only lead to a funding gap for the transition between them, but has other negative side effects as well. It exacerbates the short-term orientation of humanitarian assistance. It creates operational problems on the ground as synergies between interventions are not used and project implementation can be discontinuous. Donors are challenged by their implementing partners who often lack the expertise and capacity to operate across different forms of aid and do not coordinate their activities sufficiently with other actors (OECD, 2011).

Donors have various options and strategic decisions. They can opt for addressing one of the effects of disconnects of funding gap for transition through specialized funding instruments. This promises quick and visible results, but exacerbates the underlying problem. Alternatively, they can opt for the more arduous route of reducing the disconnect through decentralization, intra-governmental coordination, incentives for partner organizations or a combination of these measures (OECD, 2011).

Donors owe a responsibility to their funders (governments or boards) of ensuring that the funds disbursed to the recipients are used for the intended purposes. To meet this objective, disbursements are preceded by a funding agreement which stipulates how the funds will be spent among other conditions. Expenditure ceilings are thus built into these agreements to prevent misuse, align the impact and outcome of these projects to the country's` direction of

development as well as to the Millennium Development Goals (MDGs). Unfortunately, it's these very safeguards which become an impediment to the establishment of a smooth implementation and sound reporting process. Whether the projects are implemented by governments, local Non-Governmental organizations (NGOs) or the donor's own local management teams, these strict expenditure ceilings within which implementers have to operate in order to warrant a continued flow of funds from the donors, leave little room for the establishment of sound and effective reporting (Lancaster, 1999).

Utilization of donor funds had been a challenge to both the donor community as well as the agencies that are responsible for effective utilization of the same. NGOs are at the forefront in ensuring that the recipients of donor funds use the same effectively but this has not been the case. Therefore there is need for institutions that are responsible for the management of these funds to come up with the right framework and procedures in order to ensure that funds given are utilized as expected and that the funds serve the purpose (Fowler, 1995).

With an effective framework and policies governing utilization of donor funds nothing much will be expected in form of results. All relevant organizations must work in harmony if the expected outcomes are to be achieved. It is clear that there is need for coordination and collaboration among various stakeholders to ensure that funds received are made use of efficiently and effectively (Edwards & Hulme, 1995).

2.3.3 Partnerships

A partnership is a sort of collaboration to pursue common goals, while leveraging joint resources and capitalizing on the respective competences and strengths of both partners Jamali & Keshishian (2009: 279). NGOs are thought to have speed, flexibility, relative cheapness, high implementation capacity, and lack of bureaucracy in the delivery of their services. Need to reach the target group in the fastest way possible to provide assistance has forced many international Refugee Non-Governmental organizations to work with partners organizations. This has led to delegation of Authority to the Partners Organization in the programme budget implementation. Partners potentially bring to the table different strengths legitimacy, technical capacity, local knowledge, funding but they also bring along costs of coordination and various opportunity costs. The implementation of projects by Non-

Governmental Organization through local Partner organization has been supported by the following theories

Under the Stakeholder theory, if an organization is to succeed it must be able to manage and develop the relationships with its stakeholders. Organizations legitimacy and survival depends how it deals with these different and often opposing interests (Freeman, 1984). Examples of stakeholders are customers, employees, suppliers, competitors, regulators, NGOs, media and local communities (Freeman, 1984). The external pressure on companies and the risks involved in mismanagement of stakeholders have increased the companies' attention on their stakeholders (Googins and Rochlin, 2000). Some predictive academics also claim that the future society will be a "stakeholder" society where partnership within the community must be a core element of a business strategy (Elkington, 1998).

Some academics believe that social network theory is only a complement to stakeholder theory (Abzug and Webb, 1999) , but it can also be considered an individual theory as in cross-sector alliances the theory where it is considered central due to its main focus on the establishment of relations (Neergaard, Jensen and Pedersen, 2009). Each NGO possesses a distinctive network which is a resource which a partnering company can use to gain a competitive advantage (Yaziji, 2004). Social network theory indicates that organizations centrally located within the network possess unique social capital that gives them access to specific actors and resources (Tsai, 2000). The social capital is a precondition for the process of transferring and utilizing the knowledge required for the partnership to succeed. As this influences how the possible synergies from partnering will be, it can be critical for the learning and long term success of a cross-sector partnership (Arya and Salk, 2006).

The Resource dependence theory proposes that actors lacking the essential resources in their business environment will seek to establish relationships with others in order to obtain the needed resources. Organizations will also attempt to adjust their dependence relationships by minimizing their own dependence or by increasing other organizations' dependence on them. NGOs in their dependence of money, information and legitimacy should seek corporate partnerships (Yanacopulos, 2005). Yaziji mentions the following as resources in NGOs

which companies can use to gain a competitive advantage: legitimacy, awareness of social factors, distinct networks and specialized technical knowledge (Yaziji, 2004).

Transaction cost theory is also called Efficiency theory has its main focus in the savings or productivity gains through lower transaction costs when combining resources and efforts (Williamson, 1985, Austin, 2000). Company moves from a philanthropically relation with an NGO to a more alliance-based relation, it is the increase in frequency of transactions that creates the benefits of creating an alliance (Williamson, 1991, Austin, 2000). For companies operating in developing countries, transaction cost theory will advocate that the cost could be lower when working with an NGO instead of dealing with the local government (Peterson, 2010).

If a partnership does not create mutual benefits to the participating organizations, there will be a mismatch between a partner's contribution and its benefits, and this misallocation of cost and benefits are often the reason for the failure of many partnerships (Berger, Cunningham and Drumwright, 2004).

Partnership creates a much more dependent relationship between the partners, and value will only be created through a mutual exchange of ideas, resources and efforts (Googins and Rochlin, 2000). The criteria for success will often be overlapping (Neergaard, Jensen and Pedersen, 2009).

2.4 Empirical Review

The Budgeting systems are universal and have been considered an essential tool for financial planning. These systems are meant to organize and encourage the performance of non-governmental organizations (Abernethy and Brownell, 1998)

The previous 2009 global financial crisis came along with the global humanitarian crisis, what seemed to be a collapse of major financial institutions. Governments worldwide concentrated their financial resources in keeping their banks and financial institutions afloat, e.g. Britain worked on a \$87.7 billion bank recapitalization concentration on Barclays, HSBC and the Bank of Scotland, Netherlands, Belgium and Luxembourg put up approximately \$16.1 billion to save the Fortis Bank and of course the approximately \$700 billion monster

US bailout (U.S Bailout, Wichita Business Journal: Monday December 1 2008 by the Charlotte Business Journal).

The question is: how much money will be left for international aid? Some of the biggest development and Humanitarian NGOs laid off staffs or revising programmes for 2009 as their income streams flatten because of the global financial crisis. Fundraising experts of three of the world's top NGOs Oxfam GB, Save the children UK and World Vision USA said programmes growth would slow in 2009 as a result of the income squeeze (Dakar, 27 October 2008 IRIN/OCHA www.iringnews.org). Aid groups did all they could to prevent the cuts from affecting beneficiaries.

A review of the previous related studies and findings on the exchange rate and budgets have been summarized below.

Peter (2001) carried a study on budgetary controls in NGOs in Kenya. The study was to furnish a conceptual basis for evaluating the effectiveness of budgeting practices. The objective was how accurate budget anticipates the level and direction of actual results, what factors influence budget accuracy. The population of the study was a relief project spread all over the country; data was collected using primary and secondary data. It was concluded that budget controls practices in NGOs vary significantly between relief projects and development projects.

Murrison (2001) carried out a survey of budgeting practices among the major British non-governmental organizations in Kenya; he focused on budgeting practices used in British Non- governmental organizations in Kenya and the extent to which budgets are used as a management control. Data was collected from thirty relief projects of World Vision which were surveyed all over the country, the objective of the study was to determine how accurate budgets anticipate the level and direction of results, at the end of the research it was found that 100% of the Relief projects over estimates their income budgets.

Osoro (2001) in his study establishes how accurately budgets anticipate the level and direction of actual results. The analysis found out that budgetary practices in relief organization are clearly different from developmental organizations due the differences in

donor funding and reporting requirements. It established that more stringent controls exist in relief programs than in developmental ones. It is established that more complex control techniques are required in developmental programs than in relief, programs due to close donor supervision and need for monthly accountability in the later as opposed to the former whose funding is not followed with strict reporting requirements. Several other factors were found to influence the lack of effective control in developmental organizations.

Study by Kiptoo (2007) focused on the real exchange rate, volatility, and misalignment, and its impact on the Kenya's international trade, and investment. The study by Kiptoo (2007), focused on RER volatility and misalignment on international trade and investment. The study used (GARCH) and unconditional standard deviation. The study found out that RER volatility has a negative and significance impact on trade and investment during the study period 1993 to 2003.

Muthinji (2009), did a study on the challenges of budget implementation at the Commission of higher education, the objective of the study was to identify the challenges of budget implementation and its effectiveness at the Commission. Data was collected from all departments and descriptive statistics was used to summarize the data. It was concluded that a budget is important for communication and there is an increasing trend towards decentralization.

Gachithi (2010) also focused on the factors that influence budget implementation in public institutions in Kenya, a case of University of Nairobi. He used descriptive method of study and concluded that there is inefficacy in the budget preparation procedures and that the budget process faces a lot of challenges. He concluded that budgets are strong planning tool for the future.

The study by Sifunjo (2011) examined chaos and non-linear dynamical approaches to predicting exchange rates in Kenya. The study used Generalized Autoregressive Condition of Heteroscedasticity (GARCH) to measure foreign rate volatility. The results suggest presence of non-linearity in the returns, high volatility in the exchange market with a maximum duration of 6 months. Foreign exchange market was found not to be efficient in the weak form.

Adongo (2012) study sought to accomplish the following objectives; determine the salient features of budgetary controls in state corporations, establish the human factors within budgetary controls, establish the process of budgetary control in public organizations, and determine the challenges affecting budgetary control. The Relationship between budgetary control and financial performance was undertaken through carrying out a correlation analysis of the dependent and independent variables. Findings indicated that a positive relationship existed between budgetary control and financial performance of state corporations.

Gacheru (2012) in her study on the effect of budgetary process on budget variances in NGOs in Kenya sought to determine the relationship between budgeting process and budget variances in Kenyan NGOs. Based on the population of 6,075 she used a sample of 20 to collect data and descriptive data analysis and concluded that budget preparation, control and implementation significantly influence budget variance.

Study by Musyoki (2012) on RER volatility in Kenya using GARCH and computation of the unconditional standard deviation of the changes for the period of January 1993 to December 2009 found that RER was very volatile for the entire period of the study. Kenya's RER generally exhibited an appreciating and volatility trend, implying that in general, the country's international competitiveness deteriorated over the study period.

The study by Ouma (2013) examined the impact of Central Bank Intervention on Foreign Exchange rate volatility in Kenya. The study population consisted of all foreign currencies exchange rate traded at the foreign exchange markets. Results of the study conclude that the market including the central bank, the banking sector and the corporate sectors ought to develop hedging instruments to minimize speculative tendencies prevalent in the foreign exchange market. The central bank needs to intervene to smooth out the wide fluctuations in the exchange rates in order to minimize the misalignments in the exchange rates from its fundamental levels.

James (2013) carried a study on the Impact of Exchange rate on diaspora remittance in Kenya. The objective of the study was to investigate the effect of exchange rate on Kenya diaspora remittance. The population of the study was based on the average monthly exchange rates, Diaspora remittances, inflation rates and interest rates between January 2005 and

December 2012 using data from CBK and KNBS. The findings were exchange rates have an impact on the amount of remittances received in Kenya at a particular point in time. It demonstrated that at a higher level of exchange rate (Weak Kenya shillings to US dollar), more money is remitted into Kenya and when the Kenya shillings strengthens against US Dollar less money tend to be remitted into Kenya.

2.5 Summary of the Literature Review

The Budget in Non-governmental organizations is important aspects for it ensures planning and measurement of projects goals and objectives. It involves working within the costed plan of activities (budget) and taking corrective action as appropriate and revising expectations in the light of latest information. Most academic studies have focused on understanding budgeting with regard to tools, techniques, processes, control and performance while studies on Exchange rate has been centered to exchange rate volatility ,central bank monetary intervention's, diaspora remittance and balance of trade .

Kiptoo (2007) the study found out that RER volatility has a negative and significance impact on trade and investment during the study period 1993 to 2003. Sifunjo (2011) study results suggest presence of non-linearity in the returns, high volatility in the exchange market with a maximum duration of 6 months. Foreign exchange market was found not to be efficient in the weak form. Gacheru (2011) study concluded that budget preparation, control and implementation significantly influence budget variance. Ouma (2013) concluded that the central bank needs to intervene to smooth out the wide fluctuations in the exchange rates in order to minimize the misalignments in the exchange rates from its fundamental levels

The existing literature has not given much emphasis on the effect of exchange rate on budget variance of international Refugee non-governmental organizations. This study seeks to fill the research gap by establishing the effect of exchange rate variations on budget variance of International Refugee Non-Governmental Organizations in Kenya.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes design and methodology that was used in the study.

3.2 Research design

Creswell (2003) defines a research design as the scheme, outline or plan that is used to generate answers to research problems. This study adopted a descriptive research design, which according to Kothari (2004), descriptive study, is used when the problem has been defined specifically and where the researcher has certain issues to be described by the respondents about the problem. A descriptive research design determines and reports the way things are and uses a pre-planned design for analysis (Mugenda and Mugenda, 2003).

3.3 Population

Cooper and Emory (1995) defined population as the total collection of elements about which the researcher wishes to make some references. The target population comprised of the International Refugee Non-governmental organizations in Kenya. The population was drawn from a list of NGOs database of International refugee organizations duly registered by the Non-Governmental Organization Co-ordination Board of Kenya as at 31st December 2013. There were 20 International Refugee Non-governmental organizations in Kenya hence the population of study was 20.

3.4 Sample Size

The sample size was based on the international refugee organizations in Kenya data available from the NGO Co-ordination Board of Kenya and the individual organization website for the period under review as at 31st December 2013. It was restricted to four annual financial years only. That is from financial years 2010 to 2013.

3.5 Data Collection

Secondary data provided a useful source from which to answer the research question(s). Punch (1998) mentions several advantages of using existing data. For this study the

researcher used Secondary data mainly annual audited financial reports submitted to the Non-Governmental Organization Co-ordination Board of Kenya between financial years 2010 to 2013. Other secondary data were sourced from the individual organization website for the period under review. Questionnaires was be used to collect Primary data information that were not be available in the secondary data. It was gathered directly from respondents to supplement the secondary data for the purpose of this study.

3.5.1 Data Validity and Reliability

The data was obtained from the Audited Financial Statement and the Central bank of Kenya website. The financial data on Partner organization which was not available in the financial statement was obtained through questionnaire from the respective organizations. The researcher administered a survey questionnaire to each member of the target population. The questionnaire was carefully designed and tested with a few members of the. This was done to enhance the validity and accuracy of data collected for the study.

The researcher administered the questionnaires individually through email and follow up telephone calls to all the International Refugee Non-governmental organizations that formed sample population. The researcher maintained a register of questionnaires.

3.6 Data Analysis

Quantitative data collected was be analyzed by the use of descriptive statistics using SPSS and was presented through, means, standard deviations, maximums and minimum data points. The information was be displayed by use of descriptive statistics.

Statistical method of multiple regressions form below was to estimate the effect of each variable in the study to determine the relationship between the exchange rate volatility and Budget variance.

3.6.1 Analytical Model

The following regression model will be applied

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e$$

Where

Y is the Budget variance as measured by the annual amount of deviation from budget against the actual reported expenditure in US Dollars as experienced by the international Refugee non-governmental organizations in Kenya

X₁ is the Exchange Rate Volatility as measured by central bank monthly exchange rates in US Dollars.

X₂ is the amount of foreign currency funding/contracts as measured by the total annual amount of the budget funded in foreign currency in equivalent US Dollars.

X₃ is the budget portion implemented through Partners organization, as measured by comparing the annual amount of deviation from budget against the actual reported expenditure by partner organization in equivalent US Dollars.

∞ is the constant term.

e is the error term.

3.6.2 Test of significance

This study used ANOVA to test the significance by analyzing the differences between group means and their associated procedures (such as "variation" among and between groups). The observed variance in a particular variable was partitioned into components attributable to different sources of variation. ANOVA provided a statistical test of whether or not the means of several groups are equal by portioning the total variance into components that is due to true random error and the components were then tested for statistical significance.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents the information processed from the data collected during the research on the effects of exchange rate volatility on budget variance of International Refugee Non-Governmental Organization in Kenya. The population contained annual data on the budget variance, exchange rates as measured by the central bank monthly exchange rates, amount of annual foreign currency funding/ contracts and the annual amount of deviation from budget against the actual reported expenditure by partner organization in equivalent US Dollars between the years 2010 to 2013 based on the annual audited financial statements.

The chapter also presents analysis of the data and the findings based on the analysis. Data analysis was carried out using Statistical Package for the Social Sciences (SPSS). Result of the data analysis includes descriptive statistics, Pearson product moment correlation coefficient of the dependent variable and each of the independent variables and the coefficients of the multiple linear regression model.

The Primary Data used in this research was based on the Annual Audited financial statement of 8 out of 20 International Refugees Non-Governmental Organization in Kenya as registered by the NGO Coordination board of Kenya which represents 40% of the population. Secondary data was collected mainly for portion of data on budget deviation through Partner organizations where it was not clearly stated in the Audited financial statement. The monthly exchange rate data was collected from central bank of Kenya website during the four years of this research study January 2010 to December 2013.

4.2 Descriptive statistics

The tables below illustrate the number of data points used for the values obtained, the minimum and maximum values observed during the study period, the mean and standard deviation of the data under study for each of the variables.

Table 1: Budget variance experienced by International Refuge NGOs

	N	Minimum	Maximum	Mean	Std. Deviation
Budget variance	32	50560.00	2040502.07	640654.55	473752.98

The dependent variable “the budget variance” had a mean of \$ 640,654.55 and a standard deviation of \$437,752.98 over the period of the study January 2010 to December 2013. The minimum budget variance was \$ 50,560 in the year 2010 and a maximum of \$ 204,502.07 in the year 2011. This was attributed to the less volatile exchange rate fluctuation in the year 2010 as compared to the volatile exchange rate fluctuation within the year 2011 respectively. The amount of the annual funding in foreign currency contracts was low in 2010 and slightly higher 2011 also among other factors variance as a result of implementation through partner activities experienced in the country contributed to the above budget variance.

Table 2: Annual data summary of the Monthly Exchange Rate

Year	N	Minimum	Maximum	Mean	Std. Deviation
Year 2010	12	75.79	81.43	79.23	2.03
Year 2011	12	81.03	101.27	88.81	6.24
Year 2012	12	82.90	86.34	84.54	1.11
Year 2013	12	84.15	87.48	86.12	1.18

The Table 2 above illustrates the summary of monthly exchange rate data per year. Since the period of study was annually for the four years 2010 to 2013 but the central Bank of Kenya Exchange rate used in the study was available in monthly figures.

In the year 2010 the mean exchange rate was 79.23 and a standard deviation of 2.03 with a minimum of 75.79 in the month of January and a maximum was 81.43 in the month of July. In the year 2011 mean exchange rate was 88.81 and a standard deviation of 6.24, with a minimum of 81.03 in the month of January and a maximum exchange rate was 101.27 in the month of October. In the year 2012 the mean exchange rate was 84.54 and a standard deviation of 1.11 with a minimum of 82.90 in the month of March and a maximum of 86.34 in the month of January. In the year 2013 the mean exchange rate was 86.12 and a standard deviation of 1.81 with a minimum of 84.15 in May and maximum of 87.48 in August.

Table 3: Exchange rate volatility summary for the four years

	N	Minimum	Maximum	Mean	Std. Deviation
Exchange rate volatility	4	79.23	88.81	84.6725	4.03548

Over a period of four years the USD exchange rate had an annual mean of 84.67 and a standard deviation of 4.03 with a minimum exchange rate of 79.23 in year 2010 and a maximum of 88.81 year 2011. The country experienced volatile exchange rate movement within the year of 2011. It is observed that the exchange rate has risen from 2010 to 2013 and don't seem to reduce at any chance. However the volatility of the exchange rates differs within the years.

Table 4: The amount of annual budget funded in foreign currency contracts.

	N	Minimum	Maximum	Mean	Std. Deviation
Total Funding	32	565488.00	8526628.45	4681271.72	2423817.05

The annual budget proportion funded in foreign currency contracts had a mean amount of \$ 4,681,271.72 and a standard deviation \$ 2,423,817.05 with the minimum value \$565,488 in year 2010 and the maximum being \$ 8,526,628.45 in the year 2012. The study observed high proportion of budgets within the International NGOs in Kenya under this study are funded in foreign currency contracts as compared to the total budget value funded by local currency contracts in Kenya. The total value of funding has been fluctuating within the organizations thought it represents as overall increase between the years of 2010 to 2013. There was a huge gap between the highest and the lowest funded.

Table 5: The amount of budget deviation experienced by Partners organization.

	N	Minimum	Maximum	Mean	Std. Deviation
Deviation in budget of partners	28	9975.82	385252.37	91744.57	119235.69

Budget deviation from partner organizations had a mean of \$ 91,744.57, standard deviation was \$ 119,235.69 with the minimum value \$ 9,975.82 in year 2010 and the maximum being \$ 385,252 in the year 2012. The study observed that the amount of deviation from partner

budget and the portion of budgets funded through partner organization were fluctuating among the years. The grants agreements between the partner organization and international organizations were drawn in local currency.

4.3 Regression model, analysis and results

Regression analysis was meant to provide precise results on the relationship between dependent and independent variables. A multiple linear regression was used as it allows for simultaneous investigation of the effects of two or more independent variables on a dependent variable.

Table 6: Linear regression model summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.728 ^a	.530	.471	230749.30875

a. Predictors: (Constant), Amount of funding in foreign currency contracts, Exchange rate, Amount of budget deviation by partners organizations.

This data provides an R value of 0.728 which represent a high correlation. It indicates a fairly high degree of correlation which is above 0.5. The R square is the variation in the dependent variable being explained by the independent variables. The R square value is 0.53 implying that about 53% of the variation seen in budget variance is explained by the other three variables in the model. This implies also that 47% of the variation in budget variance is influenced by other variables which are not in the model.

Table 7: ANOVA

Model		Sum of Squares (10 ¹⁰)	df	Mean Square (10 ¹⁰)	F	Sig.
1	Regression	143.87	3	47.95	9.007	<0.001
	Residual	127.78	24	5.32		
	Total	271.66	27			

a. Dependent Variable: Budget variance

b. Predictors: (Constant), Amount of funding in foreign currency contracts, Exchange rate, Amount of budget deviation by partners organizations.

From Table 7 above, the results indicate that overall, the model is highly significant, $p < 0.001$. Implying that at 5% level of significance, at least one of the variables included in the model is useful in predicting budget variance to the NGO at a given time.

Table 8: Regression coefficients with Budget variance as the response variable

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	-871587.41	1058651.40		-.823	.418
Exchange rate volatility	11843.51	12581.95	.133	.941	.356
Total Funding	.072	.019	.561	3.817	.001
Amount of deviation in partners budget	.773	.388	.290	1.992	.058

a. Dependent Variable: Budget variance

The constant is the predicted value when all the other predictors are set to zero ($\beta = -871587.41$) i.e. the exchange rate volatility, the amount of foreign currency funding and the deviation in budget implemented by partners organization are all equal to zero. The exchange rate volatility is statistically insignificant (Beta=0.133, $p=0.356$). The amount of foreign currency funding is significant (Beta= 0.561, $p=0.001$). The amount of deviation in partner budget implemented by partners organization (Beta=0.290, $p=0.058$) was not statistically significant either as shown in table 8 above. The regression equation can be expressed as follows;

$$\text{Budget variance} = -871587.41 + 11843.51X_1 + 0.072 X_2 + 0.773 X_3$$

Where - X_1 Exchange rate

X_2 Amount of foreign contract funding

X_3 Amount of budget deviation on partner organization

The result of the regression shows that for a one point change in the independent variables, budget variance is expected to change by -871587.41 all others held constant. This is the intercept.

Table 9: Correlations

		Budget variance	Exchange rate	Total Funding	Deviation in budget of partners
Budget variance	Pearson Correlation	1	.269	.474**	.452*
	Sig. (2-tailed)		.137	.006	.016
	N	32	32	32	28
Exchange rate volatility	Pearson Correlation	.269	1	.162	.039
	Sig. (2-tailed)	.137		.377	.844
	N	32	32	32	28
Total Funding in Foreign Contracts	Pearson Correlation	.474**	.162	1	.279
	Sig. (2-tailed)	.006	.377		.150
	N	32	32	32	28
Deviation in budget of partners	Pearson Correlation	.452*	.039	.279	1
	Sig. (2-tailed)	.016	.844	.150	
	N	28	28	28	28

** . Correlation is significant at the 0.01 level (2-tailed).

* . Correlation is significant at the 0.05 level (2-tailed).

Analysis of the Pearson correlation between budget variance and either of the independent variables provided the outcomes in table 9. Correlation between budget variance and the independent variables was either a weak positive or a strong positive value. The data showed that there was a positive correlation between budget variance and exchange rate volatility (.269) there was a positive correlation between budget variance and total funding (.474) and also a positive correlation with amount of budget deviation by partner's organizations (0.452). This table also shows correlation between the variables for the data indicated within the study period.

4.4 Summary and Interpretation of findings

Four years data relating to eight International Refugee Non- Governmental Organization in Kenya were analyzed. The budget variance for the study period was correlated with exchange rate, amount of foreign contracts funding and the amount of budget deviation by partner organizations. Budget variance was the dependent variable, with exchange rate, amount of foreign contracts funding and the amount of budget deviation by partner organizations being

the independent variable. The study sought to enquire if any of the independent variable had an influence to budget variance.

A general multiple linear model was used to estimate the multivariate model of the relationship between the determinants and the Budget variance. In addition Correlation coefficients were used to show if at least any of the independent variables contribute to the dependent variable. This allowed for investigation of possible non- linear relationship between the independent variables and the Budget variance and to control for possible non-normal distribution data. Sensitivity analysis was performed using regression to test the relationship between parametric variables as remittance Budget variance data could be easily distorted by extreme observation (Gupta and Newberry, 1997).

The descriptive statistics indicate that the dependent variable (Budget Variance) most of the refugee's non-governmental organizations within a period of four years' experienced a budget variance with a mean \$ 640,654.55 and standard deviation of \$473,752.98. The minimum budget variance was \$ 50,560.00 in the year 2010 this could be attributed to comparatively less volatile exchange rate within the year 2010 compared with relative low amount of funding in foreign currency contracts relative to other years of the study. The maximum \$2,040,502.07 in 2011 could be attributed to the high volatility in exchange rate experienced in the year 2011 combined with relative increased amount of funding in foreign currency contracts. The amount of deviation in partner organizations budget did not have significant influence to the budget variance since they were signed in local currency and the portion of budget implemented through partner organization was relatively low compared to the overall organization budget. It can also be attributed to strict monitoring of partners budgets by the international organization.

The exchange rate for the period of four years had a mean of 84.67 and a standard deviation of 4.03. The average minimum exchange rate was 79.23 in the year 2010 which also recorded the lowest exchange value of 75.79 experienced in January 2010 over the four years of the study. The average maximum exchange rate was 88.81 in the year 2011, within the same year the country experienced a high volatility in the exchange rates recording the highest exchange rate value of 101.27 in month of October over the four year period of the study. It

is worth to note that the international NGOs do not have any control of the exchange rates movement since the rates fluctuates as a result of factors beyond their control, even though the funding and budgets are translated at an estimated predetermined rate based on each organization policy. The Exchange rate volatility has relatively reduced in volatility in the year 2012 and 2013 as compared to 2011, but has since moved in upward trend over the years from 2010 to 2013.

The amount of funding in foreign currency contracts to the NGOs had a mean amount of \$ 4,681,271.72 and a standard deviation \$ 2,423,817.05 a minimum funding of \$565,488 registered in and a maximum \$8,526,628.45 registered in the year 2012. The study observed high proportions of budgets within the International NGOs in Kenya under this study are funded in foreign currency contracts. The impact of exchange rate experienced by the organizations results from foreign currency translation. This further explains the reason why amount of funding in foreign currency contracts is significant in Budget variance since for a slight variation in exchange rate within a high proportion of funding in foreign currency contracts, it leads to significant budget variance. And for low amount of foreign funding in a volatile exchange rate may lead to less budget variance. The total value of foreign currency funding has been fluctuating within the organizations though it represents as overall increase between the years of 2010 to 2013. The study also observed that there exist a huge gap between the highest and the lowest funded organization in foreign currency.

Budget deviation from partner organizations had a mean of \$ 91,744.57, standard deviation was \$ 119,235.69 with the minimum value \$ 9,975.82 in year 2010 and the maximum being \$ 385,252 in the year 2012. This independent variable was found not to be insignificant to the dependent variable which could be attributed to the close monitoring of partners budgets by the international organizations and reduction on risk as the contract are done in local currency. The study observed that the amount of deviation from partner budget and the portion of budgets funded through partner organization were fluctuating among the years. The grants agreements between the partner organization and international organizations were drawn in local currency.

From the analysis the overall regression model was highly significant implying that at 5% level of confidence that budget variance can be predicted by the independent variables since our p-value was significant. To establish the specific independent variable that can predict budget variance regressions coefficients were computed to come up with the coefficients of each independent variable, total amount funding in foreign currency contracts was established to have a high impact and of significance to the budget variance (beta=0.561, p = 0.001). Exchange rate volatility was insignificant to the budget variance (beta=1.33, p = 0.356). The Amount of budget deviation by Partner Organization was also insignificant to the budget variance (beta=0.290, p = 0.058).

To further our study on the association between budget variance and the three independent variables a correlation analysis was computed and it shows that there is a positive correlation between the budget variance and exchange volatility meaning that if exchange volatility increases the budget variance increases. The total amount funding in foreign currency contracts also has positive correlation to the budget variance, increase in the amount of funding in foreign currency contracts also imply a respective increase in the budget variance. The amount of budget deviation by Partner Organization had positive correlation to the budget variance too.

The study shows that 53% budget variance is affected by exchange rate volatility, amount of funding in foreign currency contracts and the amount of deviation in budget implemented through the partner organizations. It implies that 47% of the variation in budget variance is influenced by other variables which were not in the model of this study.

The consistency of the findings can be compared with the results from other relative but not exactly similar studies undertaken in relation to the variables of budget variance and exchange rate volatilities. Kiptoo (2007) the study found out that RER volatility has a negative and significance impact on trade and investment during the study period 1993 to 2003. Sifunjo (2011) study results suggest presence of non-linearity in the returns, high volatility in the exchange market with a maximum duration of 6 months. Foreign exchange market was found not to be efficient in the weak form. Gacheru (2011) study concluded that budget preparation, control and implementation significantly influence budget variance.

Gacheru (2012) in her study on the effect of budgetary process on budget variances in NGOs in Kenya sought to determine the relationship between budgeting process and budget variances in Kenyan NGOs, concluded that budget preparation, control and implementation significantly influence budget variance. Ouma (2013) concluded that the central bank needs to intervene to smooth out the wide fluctuations in the exchange rates in order to minimize the misalignments in the exchange rates from its fundamental levels.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents summary, conclusion and recommendations. The descriptive statistics data results of the study were presented in table's summary of mean and standard deviation of different variables in the study. Maximum and Minimum values of the variables were also provided. A multiple linear regression model was used for data analysis; the output demonstrated the correlation between the dependent variable (Budget variance) and the independent variables exchange rates, amount of funding in foreign contracts and amount of budget deviation experienced by partner organizations. R square value was illustrated which indicated the variation of dependent variable explained by the independent variables. Based on the findings in chapter four, the study gives recommendations after which it draws the policy recommendations.

5.2 Summary

The objective of the study was to establish the effects of exchange rate on budget variance of international refugee non-governmental organizations in Kenya. Mainly Secondary data was obtained from the audited financial statement and the central Bank of Kenya website. Primary data on Partners organization Budget deviations was used to supplement the study. This was a descriptive study using data on the Budget variance, exchange rates, amount of funding in foreign contracts and amount of budget deviation experienced by partner organizations for a period of four years based on the Audited financial statements of International organizations only and monthly average data for exchange rate obtained from the central bank of Kenya.

The study found that the Exchange rates volatility is positively related to the Budget Variance with coefficient of correlation of 0.269. However, at 95% confidence level, the effect of Exchange Rate Volatility on the budget variance was not significant (P value of 0.356). Total amount funding in foreign currency contracts also has positive correlation to the budget variance, with coefficient of correlation of 0.474 and significant at 95 confidence level (P value of 0.01). Further, the amount of budget deviation by Partner Organization had

positive correlation to the budget variance with coefficient of correlation of 0.452. However, at 95% confidence level, the effect of amount of budget deviation by Partner Organization on the budget variance was not significant (P value of 0.058).

The researcher found out that exchange rate had an insignificant effect on budget variance of international refugee non-governmental organizations in Kenya. Amount of funding in foreign currency contracts had a significant effect on budget variance. The amount of budget deviation experienced by partner organizations had an insignificant effect on budget variance. The variables affect budget variances in variable degrees. However the variable used in the study only represents a percentage of factors that affect budget variance. For the purpose of this study three variables were considered significant and sufficient.

5.3 Conclusion

The study investigated the effects of exchange rate on budget variance of international refugee non-governmental organizations in Kenya. The conclusion derived through the findings was that exchange rates have a relationship with the budget variance experienced by the international non-governmental organizations. The finding demonstrated that during period of high volatility in exchange rates, organizations experienced relative increased variance in the annual budget. This was complimented by the high proportion of funding of the international organizations in foreign currency contracts. This means for each slight change in exchange rate for an organization with high funding in foreign currency contracts there was significant change in the budget variance experienced.

The study also concluded that there are other factors that affect the budget variance which are not necessarily exchange rates or variables within this study. The findings are consistent with Gacheru (2012) in her study on the effect of budgetary process on budget variances in NGOs in Kenya sought to determine the relationship between budgeting process and budget variances in Kenyan NGOs, concluded that budget preparation, control and implementation significantly influence budget variance.

5.4 Policy Recommendations

The international non-governmental organizations in Kenya should recognize and factor the impact of exchange rates on their high proportion of funding in foreign currency contracts which further has a significant effect on the budget variance. It is worth noting that annual budget variance recorded by organizations is a reflection of their efficiency in monitoring and controlling their budgets. The funding for these organizations keep on fluctuating and are awarded based on restrictive agreements. Organizations should ensure they maximize their financial performance by reducing the impact of budget variance. Clear Policy documents to ensure close monitoring and control of the effects of budget variance should be put in place to mitigate the impact of the budget variance.

A stable exchange regime will lead to better planning by the international organizations. It will lead to better estimation of budget rates against the actual exchange rates on the market. The government needs be sensitive to the impact of the exchange rate volatility to the overall economy, to improve on the existing policy and implement it to ensure the country undergo a stable exchange rate regime. Efficiency of the financial markets should be improved to allow for the prediction and estimation of exchange rates prevailing in the market and discourage speculative or manipulative tendency by either commercial banks or other actors in the financial markets. More information needs to be disseminated to the public, to strengthen the supervisory bodies like the central bank of Kenya.

The study reveals the high proportion of foreign currency contracts funding to international Non-governmental organization in Kenya. With the ongoing public debate on the proposed bill in the parliament of Kenya for discussion to curb and regulate the Non-governmental organization foreign currency contracts funding at 15% of their budget, Non-governmental organization should lobby and monitor the discussion closely as the impact of such regulation will impact heavily to their continued operations in Kenya. The international Non-governmental organization in Kenya should develop contingency strategic plan to source and fund their budgets encase the bill goes through.

5.4 Limitations of the study

It was noted that only a fraction of the factors affecting budget variance formed the subject of the study. The model used in this study has therefore not brought in other factors. Due to lack of resources and data on the other factors, it was not possible to include more variables in this study. This was partly because there has been limited study on the impact of exchange rate on international non-governmental organizations in Kenya since most studied has concentrated on the budget process and budget performance. This led to limited information about effects of exchange rate volatility among the international non-governmental organizations in Kenya.

The data used was from the Central Bank of Kenya. The data from the Central Bank of Kenya are market averages and are indicative rates. They were monthly average rates from Central bank and not daily rates. The commercial bank exchange rate vary from one bank to another and the daily rates used to transact the hard currency and currency conversion by the international organization are not exact to the central bank rates. The information should therefore be used with caution bearing these dynamics.

The study only analysed a period of four years for 2010 to 2013. Since the period covered was short, generalizing the findings may be hard in addition to findings being different if longer period was analysed. The study also did not adjust the data obtained to remove seasonal fluctuations which may distort findings.

5.6 Suggestions for further Studies

As noted in this study, the variables used form only a fraction of the factors affecting Budget variance of International Refugee Non-Governmental organizations in Kenya. It will be of interest to identify the other factors which were not considered in this study. This will give a holistic picture of the factors affecting the budget variance of International Refugee Non-Governmental organizations in Kenya.

Value of transaction in local currency represents a significant portion of the operational budget of International Refugee Non-Governmental organizations in Kenya. A further study

can be undertaken to investigate what contribution does value of transaction in local currency has on the budget variance in relation to exchange rates volatility.

It will be worth to study how different international non-governmental organizations mitigate on their exchange rate risks by investigating the impact of the organization policy and control on the exchange rate risks exposure.

This study investigated the effect of exchange rate on the organization annual budget variance. Further study can be done to establish the impact of exchange rate to specific donor grants e.g. European Union which has strict rules regarding exchange rates in the management and reporting of its grants.

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APPENDICES

Appendix I: Letter of Introduction

To whom it may concern

Dear Sir/Madam,

INTRODUCTION LETTER

REF: MOSES JUMA OKUMU – D61/79120/2012

I am a post graduate student at the University of Nairobi pursuing a master's degree in Business Administration. In addition to the pre-requisite course work, I am carrying out a research project to establish the effect of exchange rate volatility on the budget variance among the International Refugee Non-Governmental Organizations in Kenya. The study will be carried out among the International Refugee Non-Governmental Organizations in Kenya that are registered member with the Kenya Non-Governmental Organizations Coordination Board. The findings will be confidential and will be strictly used for academic purposes. Your name or your institution will at no time appear in my report a copy of the final report can be availed to you upon request.

For any further clarification or concern about the study, please ask or contact the researcher on Email: moses.okumu@hotmail.com

Your authorization and assistance will be highly appreciated.

Yours sincerely,

Moses Okumu

MBA Student University of Nairobi.

Appendix II: Questionnaire

Part A: Demographic information

1. Department:
2. What is your designation?
3. What is the length of time you have worked in the organization?

PART B: EFFECT OF PARTNERS ORGANIZATION ON THE BUDGET DEFICT

1. Do you involve ‘Partner’ organization in implementing your programs?
 Yes [] No []
2. What is the contract currency for your local partner organization grants agreement?
 Local currency [] Foreign Currency []
3. What was the total amount of deviation on the annual budget against the expenditure reported by your ‘Partner’ organizations in the following financial years?

	2010 (\$)	2011 (\$)	2012 (\$)	2013 (\$)
Annual Budget				
Annual Expenditure				
Budget Deviation				

Thank You

Appendix III: Central Bank of Kenya US Dollar rates

MONTH, YEAR	CBK Mean Monthly US Dollar Exchange Rate
Dec, 2013	86.31
Nov, 2013	86.10
Oct, 2013	85.31
Sep, 2013	87.41
Aug, 2013	87.48
Jul, 2013	86.85
Jun, 2013	85.49
May, 2013	84.15
Apr, 2013	84.19
Mar, 2013	85.82
Feb, 2013	87.45
Jan, 2013	86.90
Dec, 2012	85.99
Nov, 2012	85.63
Oct, 2012	85.11
Sep, 2012	84.61
Aug, 2012	84.08
Jul, 2012	84.14
Jun, 2012	84.79
May, 2012	84.46
Apr, 2012	83.19
Mar, 2012	82.90
Feb, 2012	83.18
Jan, 2012	86.34

MONTH, YEAR	CBK Mean Monthly US Dollar Exchange Rate
Dec, 2011	86.66
Nov, 2011	93.68
Oct, 2011	101.27
Sep, 2011	96.36
Aug, 2011	92.79
Jul, 2011	89.90
Jun, 2011	89.05
May, 2011	85.43
Apr, 2011	83.89
Mar, 2011	84.21
Feb, 2011	81.47
Jan, 2011	81.03
Dec, 2010	80.57
Nov, 2010	80.46
Oct, 2010	80.71
Sep, 2010	80.91
Aug, 2010	80.44
Jul, 2010	81.43
Jun, 2010	81.02
May, 2010	78.54
Apr, 2010	77.25
Mar, 2010	76.95
Feb, 2010	76.73
Jan, 2010	75.79

Appendix IV: List of International Refugee NGO in Kenya at the NGO Coordination Board as at 31st December 2013

1. Abizeramariya Kenya
2. Church World Services and Witness
3. Danish Refugee Council
4. Humanitarian Africa Relief Development Organization
5. International Association for the Marginalized Children
6. International Medical Corps
7. International Rescue Committee
8. Lutheran World Relief - East Southern Africa Regional office
9. Mennonite Board in Eastern Africa
10. Norwegian Church Aid
11. Norwegian Refugee Council
12. Peace Building, Healing and Reconciliation Programme
13. Refugee Point International
14. Romania Direct Help- International Direct Help
15. Samaritans Purse International Relief
16. St. Michael Community Development International
17. The African Centre for Empowerment Gender and Advocacy.
18. The Regional Centre for Community Welfare and Extension
19. Trocaire
20. World Vision Kenya