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Original Article

Does the Legal Framework Moderate the Relationship between Resource Allocation Reforms and Financial Performance of County Governments? Evidence from Kenya

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Resource Allocation, Budgetary Control, Budget Planning, Budget Absorption, Legal Framework, County Government Financial Performance.

ABSTRACT

This study examined the effect of resource allocation reforms on the performance of county governments and how the legal framework moderates this relationship. The study was grounded on resource allocation theory, informed by positivist research philosophy and utilized a correlational research design. The target population consisted of the 47 county governments in Kenya, which were clustered into seven regional blocs. Within each regional bloc, a county with the lowest budget absorption rate, as per the Controller of Budget's 2023 report, was selected. The top and middle-level management employees in the Department of Finance and Economic Planning were selected resulting in 229 target respondents upon which a sample size of 144 was determined using Krejcie and Morgan formulae. Data was analyzed using the SPSS Analysis of Moment Structure, employing factor analysis and structural equation modelling. Results of the study revealed that resource allocation reforms had a statistically significant effect on County financial performance, (β=0.499, t=5.578, p< 0.05). However, the legal framework in place had an insignificant moderating effect on the relationship between resource allocation reforms and County financial performance (β=0.019, t=0.225, p> 0.05). The paper concludes that issues relating to reforms targeting resource allocation are important in improving the financial performance of county governments and recommends effective implementation of resource allocation reforms to ensure enhanced performance of county governments in Kenya.

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INTRODUCTION

The financial performance of any public institution is a matter of significant concern in Kenya. It is characterized by numerous challenges that significantly influence its corporate governance and citizen's service delivery. In Kenya, County governments were established with the sole intention of improving the provision of public services. However, counties have encountered numerous obstacles in fulfilling this mandate. This is evidenced by several key indicators such as low revenue collection rates, inefficient utilization of development budgets, a persistent increase in pending bills and a lack of adherence to predefined spending limits. Moreover, the revenue collection trend has been significantly declining between 2018 and 2023. Over this period, 76.6 percent of the 47 counties have exceeded the threshold of spending 35 percent of their revenues on personnel emoluments, thereby breaching the stipulated limit on county expenditure for these purposes. According to the controller of budget report of 2023, about 74.5 percent of the counties allocated less than 30 percent of their budgets to development projects during the same period. Furthermore, after the completion of the financial year 2021/2022, all the counties had accumulated pending bills totalling Ksh.161.4bn. Out of this, Ksh. 33.9bn was earmarked for development projects, while Ksh.127.4bn was allocated for recurrent expenses, (Government of Kenya, 2023). The objective of these reforms was to tackle the county governments' financial performance issues. Despite the implementation of resource allocation reforms, the performance of county governments has not yet reached the anticipated optimal levels. This raises questions as to the influence of these reforms on county government financial performance, an issue which this paper tries to address.

Aims of the Study

The purpose of this paper was to:

- Examine the effect of resource allocation reforms on the performance of county governments in Kenya.
- To investigate the moderating role of the legal framework on the influence of resource allocation reforms on the financial performance of county governments in Kenya.

Two hypotheses were tested: one, there is no statistically significant influence of resource allocation reforms on the financial performance of county governments in Kenya, and two, the legal framework does not statistically and significantly moderate the influence of resource allocation reforms on the financial performance of county governments in Kenya.

REVIEWED LITERATURE

The theoretical underpinning for this work was based on the Resource-Based Theory advanced by Barney (1996) who postulated that an organization's competitiveness is dictated by the extent of resources it possesses. The theory is applied in determining the nature of resources that

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an organization can adopt to acquire a competitive edge, and the emphasis of the theory is on firms' internal resources. Firm resources form the basis for developing firm capabilities, which can result in sustained superior performance over time. The theory maintains that a firm's resources include human, financial, technological, and physical resources. These resources are imperfectly mobile and heterogeneous. The management of an organization is required to understand and engage these resources in a manner that leads to attaining a sustainable competitive advantage. Barney proposes key managerial tasks related to resources, which include identifying the organization's key resources, assessing resources using VRIN criteria (valuable, rare, imperfectly imitable, and non-substitutable), and developing, nurturing, and safeguarding the resources that pass this evaluation (Holdford, 2018).

Resource allocation is the assignment of available resources to various units, departments, programs, and projects within an organization. Arsallya, Azwardi and Yusnaini (2021) studied capital expenditures and their relationship and implications on financial performance in Provinces in Indonesia and established a positive relationship between local revenue and capital expenditure. On the other hand, economic growth, adequate budgets, and surplus budget calculation positively affected the government's capital expenditures. This finding aligns with Pandya's (2017) research conducted in developed countries. Consequently, applying these findings to developing economies, such as Kenya, poses challenges due to differing economic contexts and conditions. The disparity in economic environments means that while the correlation observed in developed nations is insightful, it may not fully translate to or predict outcomes in developing countries. Correa, Osborne and Lisboa (2021) found in a study of Mayoral leadership and resource allocation in Brazilian local government that all the stakeholders have influence in decision-making regarding government expenditure and investments in infrastructure. It was further established that Mayors are not the sole decision-makers despite being at the peak of the provincial administration. The stakeholders shape the resource allocation decisions in local government.

Moreover, Ehiorobo (2018) examined resource allocation efficiency and its utilization in Nigeria to determine how resources have been utilized to attain development goals. It was discovered that there are a lot of resource allocation inefficiencies as well as wastefulness in spending because of bad governance, lack of accountability, and corruption. The implication is that, in the presence of planning, implementation, monitoring, and control, allocation and utilization are efficient. The resource allocation activity positively influenced performance as it resulted in an increase per capita and equality in resource distribution. Nurfadila (2024) analyzed public financial management by integrating performance evaluation with cost systems. The results highlight that merging the evaluation of an institution's performance with systems for cost management can lead to enhanced financial management in the public sector. This integration delivers detailed and comprehensive data that is crucial for making informed decisions, fosters more efficient resource allocation, and pinpoints areas needing improvement.

Additionally, Mohamed (2018) examined the experiences and challenges faced by counties in Kenya during the allocation of resources by analyzing the budgets of fifteen county governments. The counties were selected based on the stratification of urban counties, developed counties, and developing counties and focused on the county government's devolved functions. The study established a consistent resource allocation which was sufficient for the devolved functions though there was no formula applied in sharing the resources. The allocation of resources prioritized health, water and agriculture. It was further discovered that there is an absence of policy and procedure to guide the allocation of resources to county projects. These findings contrast with those

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of Kariuki (2019) who discovered that resource allocation is guided by policy guidelines and set objectives and that it influences decision-making. The author's objective was to establish the allocation of resources and understand the challenges in revenue allocation while determining measures which can be implemented by the Laikipia County. The study used primary data and established that resource allocation was guided by the policy guidelines and that project feasibility study improves decision-making and enhances project performance. To improve resource allocation in the county government, the study established a need for risk assessment, public participation, adequate monitoring, and effectiveness in communication. The outcome of the research is consistent with those of Mutambuki and Kabui (2022), who exposed in their study on the allocation of resources and service delivery that the allocation of resources significantly impacts service delivery.

In the same breath, Luvisi and Ondiek (2021) conducted a comparative analysis of resource allocation and absorption rates in County Governments, focusing on the Western Region which included Busia, Bungoma, Vihiga and Kakamega counties. The study targeted the finance and economic planning executive committee members and chief officers. Panel data from 2015-2019 was analyzed and results did not prove that resource allocation and absorption rate in Western Kenya's county governments are correlated. It was concluded that the absorption rate does not necessarily imply performance. Lastly, Muthomi (2021) established a contradictory finding of a positive correlation amid economic growth, annual budget and absorption rate and revenue performance.

METHODOLOGY

This paper employed a correlational research design to determine the relationship between resource allocation reforms and financial performance of county governments in Kenya indicating whether alterations in one variable coincide with corresponding changes in the other reference variable. The study targeted 229 top and middle management staff in the selected county governments out of which 144 were sampled. This paper used primary data collected using five-point Likert-scaled questionnaires.

The collected data underwent scrutiny to identify and correct errors to ensure clarity and analyzed using SPSS Analysis of Moments Structure (AMOS) for factor analysis involving exploratory and confirmatory factor analysis, similar to Ochieng' & Onyuma (2022). Resource allocation reforms variable was measured using budget planning, budget control and equitable resource allocation hence the hypothesized structural equation was as follows:

$Y_i = \alpha_0 + \beta$ * Budget planning + ε……………………………………….…………… (1)

$Y_i = \alpha_0 + \beta$ * Budget control + ε……………………….…………………………..…. (2)

$Y_i = \alpha_0 + \beta$ * Equitable resource allocation + ε……………...………………………..……..…. (3)

The legal framework was then interacted with the resource allocation reform to measure any moderation of the relationship between the effect of resource allocation on the financial performance of county governments.

Cronbach's alpha was used in testing reliability. The variables had Cronbach's alpha value greater than 0.7 confirming the reliability of the instrument. Discriminant or divergent validity assesses the extent to which measures of different constructs are distinct from one another and that they do not correlate too highly. It assesses the uniqueness of one component compared to the other in the model. The conditions for discriminant validity were achieved and the results are shown in Table 1 below.

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Table 1. Reliability and Validity of the Research Instrument

	Reliability	Convergent Validity	Discriminant Validity		
Construct	Cronbach	AVE	RAR	LF	PER
Resource allocation reforms (RAR)	0.73	0.86	**0.93**		
Legal Framework (LF)	0.71	0.69	-0.08	**0.83**	
Financial Performance (PER)	0.81	0.70	0.66	-0.03	**0.84**

It therefore means that the data was fit for analysis. The paper then proceeded with the data analysis.

RESULTS

This paper performed structural equation modelling and hypothesis testing. The paper utilized structural models for latent variables and used structural equation modelling to assess the hypothesized relationships. To evaluate the contribution of each of the indicators to each component, the paper applied regression weights helping to understand the nature of the relationship between all variables. The calculated t-values were compared against the critical |t|-values of 1.96, which corresponds to the p-value of 0.05.

Measurement Model Fitness Evaluation

Such a model fitness test was crucial for assessing how effectively a statistical model aligns with the data it intends to measure, as it determines whether the model's structure accurately captures the underlying relationships among variables (Kharuddin et al., 2020). Chi-Square (CMIN) test statistics were used to assess the overall model fitness. However, as argued by Yaslıoglu and Yaslıoglu (2020),

The CMIN test is sensitive to the size of the sample. To mitigate this risk, the paper used CMIN with other fit indices, which included the Adjusted Goodness of Fit Index (AGFI), Normed Fit Index (NFI), Comparative Fit Index (CFI) and Root Mean Square Error of Approximation (RMSEA) statistics, as recommended by Schumacker and Lomax (2004). The model fitness test results presented in Table 2 for all variables suggest that the various thresholds were attained and concluded that the model fits the data well.

Table 2. Model Fitness Test Result

Variable	CMIN	CMIN/DF	DF	AGFI	CFI	NFI	RMSEA
Resource Allocation Reforms	12.16	1.520	8	0.92	0.99	0.97	0.066

The indices for all four independent variables for the chi-square ratio fell within an acceptable range of between 1 and 5, indicating a reasonable fit. The indices for Adjusted Goodness of Fit, comparative fit index and Normed Fit Index were all above the threshold of 0.8 for the independent variables indicating the fitness of the model. According to McDonald & Ho (2002), an AGFI coefficient of 0.8 or greater is deemed appropriate. According to Tabachnick, Fidell and Ullman (2013), CFI values similarly vary from 0 to 1, with values of 0.8 or above typically considered acceptable Further, Hu and Bentler (1999) suggest that an NFI score of 0.8 or above typically suggests a good fit of the model. The RMSEA values indicated goodness of fit as they all fell below the acceptable maximum threshold of 0.1 affirming model fitness. Hu and Bentler (1999) defined acceptable boundaries for RMSEA from 0.08 to 0.10 as acceptable, with values from 0.05 to 0.08 being good and values less than 0.05 being excellent.

Structural Equation Modelling of Resource Mobilization Reforms on County Performance

Prior to structural modelling, exploratory factor analysis was carried out to evaluate whether the

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selected indicators had significant loading on the construct. We retained eight measurement items of resource allocation reforms that had a factor loading of greater than 0.7.

Table 3: Factor Loadings for Resource Mobilization Reforms

Resource Allocation Reforms Indicators	Loadings
Budget Planning (RAR1)	
The BP6-Budget planning process is effective.	.787
BP3-Budgetary allocations are based on priorities in the county multi-annual development plan.	.744
Budgetary Control (RAR2)	
BC5- There are reports prepared and presented to management by the budgetary committee on budget performance.	.844
BC4- There is an established budget performance monitoring committee.	.840
BC1- Mechanisms for budget implementation, monitoring and evaluation exist.	.768
BC7-The resource allocation has a direct influence on the performance	.753
Equitable Resource Allocation (RAR3)	
ERA3- Resources are timely disbursed to various departments in the county.	.877
ERA4-There are funds allocated to cater for emergencies or opportunities.	.811
ERA2-County resource allocation criterion is strictly adhered to.	.804

The paper also aimed to investigate the null hypothesis which stated that resource allocation reforms do not statistically and significantly affect county performance. The analysis results revealed a significant correlation between resource allocation reforms and performance ($t = 5.578$, $p < 0.05$). The impact of resource allocation changes was shown to have a path coefficient of $\beta = 0.499$, suggesting statistical significance. As a result, this null hypothesis was not accepted in favour of an alternate hypothesis, concluding that resource allocation reforms had a statistically significant effect on performance. The t-value of 5.578 exceeded the threshold $|t|$-value of 1.96, indicating that performance goes up by 0.499 units for every single unit rise in resource allocation reforms. These findings align with Mutambuki and Kabui (2022), who found that resource allocation significantly impacts service delivery, thereby reinforcing the Resource-Based Theory, which posits that the level of competitive advantage in an organization is predicted by the level of resources. In contrast, Luvisi and Ondiek (2021) conducted a comparative analysis in Western region county governments and found no correlation between resource allocation and absorption rates. The author concluded that absorption rates do not necessarily reflect changes in the performance of county governments.

From the findings, it is inferred that resource allocation reforms lead to a more strategic distribution of resources, ensuring that the most critical areas receive sufficient support, which in turn boosts overall performance and citizen satisfaction. Furthermore, effective resource allocation can reduce waste and redundancy, resulting in more efficient operations and improved outcomes. Additionally, these reforms may have aligned resource distribution with key priorities and strategic goals, ensuring that investments within the county directly enhance performance. Therefore, this paper supports the Resource-Based Theory by highlighting the importance of resource levels in influencing organizational performance.

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Table 4: Regression Weights and C.R Values

			Estimate	S.E.	C.R.	P
Performance	<-	Resource Allocation	.499	.089	5.578	***
Equitable resource allocation (RAR3)	<-	Resource Allocation	1.000			
Budgetary control (RAR2)	<-	Resource Allocation	.813	.057	14.155	***
Budget planning (RAR1)	<-	Resource Allocation	.735	.068	10.890	***
Operating surplus/deficit (PER1)	<-	Performance	1.000			
Budget absorption (PER2)	<-	Performance	.929	.118	7.895	***
Compliance to expenditure limits (PER3)	<-	Performance	.893	.102	8.714	***

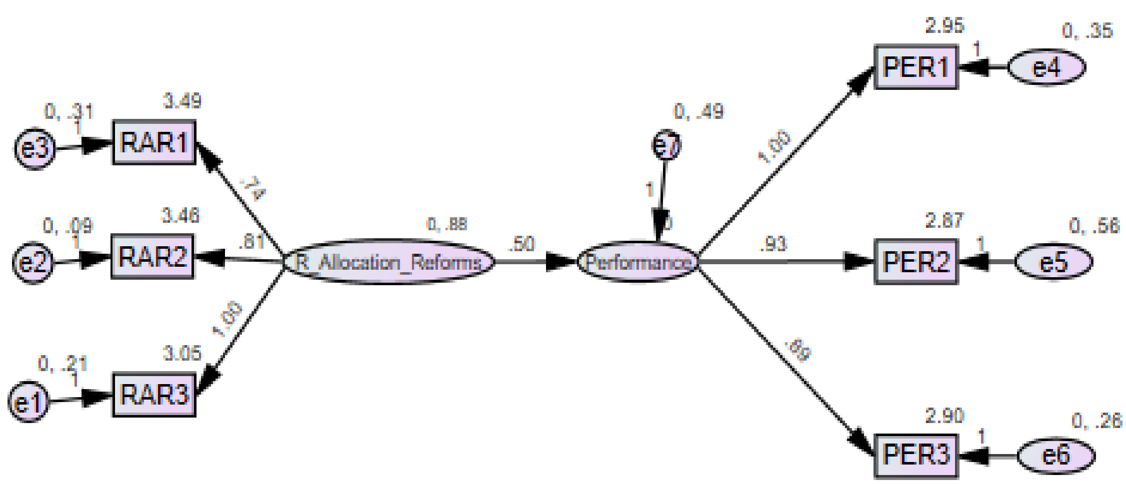
Additionally, the intercepts for each observed variable indicate the expected value of that variable when the corresponding latent variable is zero as outlined below.

Table 5: Regression Intercepts for Resource Allocation Reforms

	Estimate	S.E.	C.R.	P
Equitable Resource Allocation (RAR3)	3.055	.095	32.185	***
Budgetary Control (RAR2)	3.461	.075	46.367	***
Budget Planning (RAR1)	3.492	.081	43.302	***
Operating surplus/deficit (PER1)	2.951	.094	31.480	***
Budget absorption (PER2)	2.869	.098	29.158	***
Compliance with expenditure limits (PER3)	2.902	.083	35.072	***

The findings show that all the intercepts were positive and significantly correlated with the dependent variable, as indicated by high critical values and low p-values. The path diagram presented in Figure 1 illustrates the hypothesized structural relationships between resource allocation reforms and the performance of county governments.

Figure 1: Path Coefficients for Resource Allocation Reforms and Performance



The following Structural Equations were therefore fitted;

$Y_i = 3.492+0.740\ \lambda + 0.499$ * Budget Planning + ε…………………………………. *(4)*

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$Y_i = 3.461 + 0.810\lambda + 0.499*$ Budgetary Control+ ε………………………….……………… *(5)*

$Y_i = 3.055 + 1.000\,\lambda + 0.499$ * Equitable Resource Allocation + ε……………………*(6)*

Moderating Effect of Legal Framework on Measured Relationships

The moderating effect of the legal framework was assessed by introducing an interaction term between resource allocation reforms and the legal framework. The coefficient of the interaction term was 0.019 with a calculated t-value of 0.225 and a p-value of 0.822. This value was smaller than the |t|-value of 1.96 indicating statistically insignificant. This finding suggests that the effect of resource allocation reforms on performance is not significantly moderated by the underlying legal framework. Therefore, the paper failed to reject the null hypothesis that the legal framework does not significantly moderate the relationship between resource allocation reforms and performance. This finding is consistent with those of Gichuki, Karanja and Atikiya (2024) who did not establish a moderating role of the legal framework on organizational structure and implementation of devolved units' strategic plans in Kenya. Conversely, Karama (2022) established a positive and significant moderation effect of the legal framework and strategic planning and devolved service delivery.

This finding suggests that resource allocation reforms can be effective regardless of the legal context. Policymakers should therefore prioritize optimizing resource allocation strategies instead of solely focusing on legal adjustments. Additionally, the absence of moderation effect may be due to an established resource allocation process that functions well even within legal constraints, or it could indicate that a strong legal framework is already in place in the sampled counties.

Table 6: Moderated Regression Weights and C.R Values

		Estimate	S.E.	C.R.	P
Performance	Resource Allocation	.493	.093	5.308	***
Performance	Legal Framework	-.033	.118	-.276	.782
Performance	ZRAR_X_ZLF	.019	.083	.225	.822
Equitable resource allocation (RAR3)	Resource Allocation (R_A_R)	1.000			
Budgetary Control (RAR2)	Resource Allocation (R_A_R)	.814	.057	14.225	***
Budget Planning (RAR1)	Resource Allocation (R_A_R)	.737	.067	10.928	***
Existence and sufficiency (LF3)	Legal Framework	1.000			
Effectiveness and impact (LF1)	Legal Framework	1.000			
Operating surplus/deficit (PER1)	Performance	1.000			
Budget absorption (PER2)	Performance	.926	.117	7.889	***
Compliance to expenditure limits (PER3)	Performance	.891	.102	8.724	***

Source; Data Analysis (2024)

The path diagram presented in Figure 2 illustrates the hypothesized structural relationships between resource allocation reforms and the performance of county governments including the moderating effect of the legal framework.

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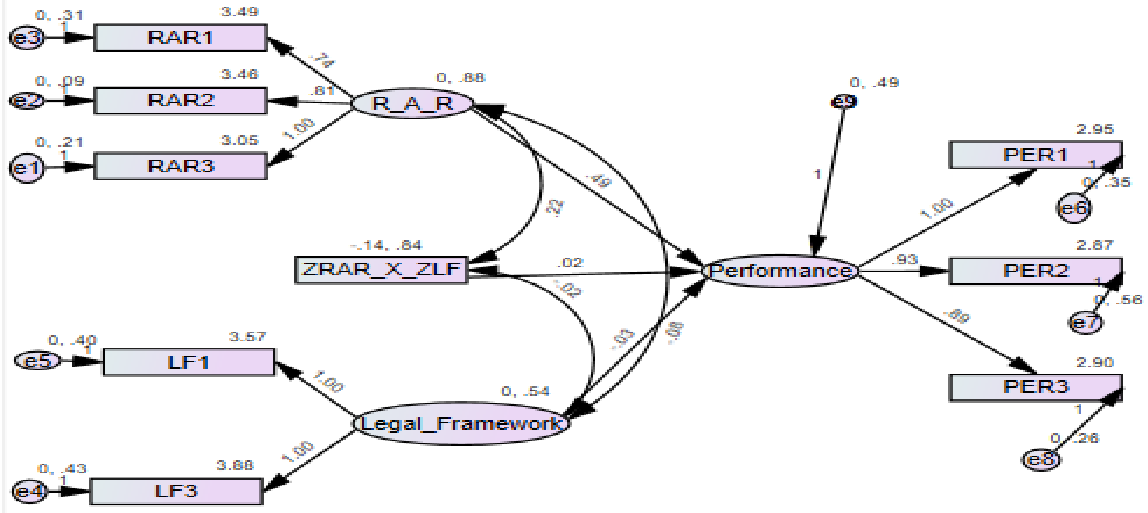
Figure 2: Path Coefficients for Legal Framework, Resource Allocation Reforms and Performance



CONCLUSION AND RECOMMENDATIONS FOR POLICY

This paper sets out to investigate the effect of resource allocation reforms on county governments' financial performance. It was observed that county governments take into consideration both expected revenue collection and equitable shares from the national government during planning. Additionally, opinions of respondents were somewhat divided regarding whether budgetary allocations align with the priorities outlined in the counties' multi-annual development plan. Furthermore, the paper established a moderate confidence that budget planning significantly influences performance in devolved county governments. Moreover, it was ascertained that the effectiveness of the budget planning process by the county governments was not very effective as a small portion of the respondents confirmed the presence of mechanisms for budget implementation, monitoring, and evaluation are in place. Most of the county governments have not implemented mechanisms to aid in monitoring and evaluation of budget implementations, however, for the counties that have implemented this mechanism, respondents confirmed its effectiveness. There was a lack of frequent reviews by the county governments to ensure that budgets were addressing the changing society's needs.

Furthermore, the presence of a budgetary monitoring committee was perceived by the respondents as positive, and the committees have always prepared and presented reports to county management for decision-making. The effectiveness of the committee was affected by a lack of timeliness in providing feedback on decision-making. Additionally, it was confirmed that the county government's budget is executed in line with the County Assemblies' approval, ensuring adherence to legislative oversight. There was a general view of the process of equitable resource allocation as fair even though not many respondents reported that strict criteria for resource allocation are consistently followed. Timeliness of resource disbursement was a concern to most of the respondents with fewer numbers, noting prompt allocation. Efforts to ensure regional balance and inclusiveness in budget formulation are also acknowledged by respondents and further the inadequate allocation of resources to emergencies or unforeseen opportunities. It was further established that there is a moderate belief that county budgeting has been effective in ensuring regional balancing and adequate distribution of county resources across the various county functional areas. Through structural equation modelling, resource allocation reforms and the performance of county governments were positively and significantly

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correlated. Furthermore, the legal framework did not have a moderating effect between resource allocation reforms and the performance of county governments in Kenya.

Based on the findings, the paper makes the following recommendations.

It is recommended that:

- The counties should address issues related to delays in the disbursement of financial resources and ensure that budgetary allocations are consistently aligned with the strategic priorities outlined in county governments' development plans.
- Finally, there is a need to promote transparency in how county government resources are allocated and utilized as well as putting in place effective monitoring and evaluation mechanisms to ensure compliance with the set policies.

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