Journal DOI: 10.36713/epra1013 | SJIF Impact Factor (2026): 8.748 ISSN: 2347-4378
EPRA International Journal of Economics, Business and Management Studies (EBMS)
Volume: 13 | Issue: 11 | November 2026 -Peer-Reviewed Journal

BUDGET PLANNING, ORGANIZATION SIZE AND FINANCIAL PERFORMANCE OF THE TOP 100 SMALL AND MEDIUM ENTERPRISES IN KENYA

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Article DOI: https://doi.org/10.36713/epra32076
DOI No: 10.36713/epra32076

ABSTRACT

Budget planning is widely promoted as a foundation of sound financial management in small and medium enterprises (SMEs), yet the strength of its payoff may depend on the scale at which an enterprise operates. This study examined the effect of budget planning on the financial performance of the top 100 SMEs in Kenya and determined the moderating effect of organization size on this relationship. The study was anchored on Incremental Budgeting Theory and Activity-Based Costing Theory and adopted a descriptive research design. A census of the 100 SMEs on the Ministry of Trade 2021/2022 list was attempted, with the Chief Accounting Officer of each firm as the respondent. Data were collected using a structured questionnaire on a five-point Likert scale, and 83 questionnaires were returned (83.0% response rate). The instrument was reliable in a pilot study (Cronbach's alpha: budget planning 0.810, organization size 0.731, financial performance 0.713). Data were analysed in SPSS using descriptive statistics, Pearson correlation and regression with an interaction term. Budget planning was moderately practised (mean = 2.81, SD = 1.054), with strong strategic alignment and budget reviews but weak forecasting accuracy, departmental participation and contingency planning (means below 2.00). Financial performance was moderate (mean = 2.90). Budget planning correlated positively with financial performance ($r = 0.678$, $p < 0.01$) and had a positive and significant effect ($\beta = 0.325$, $t = 3.779$, $p < 0.001$). The interaction between budget planning and organization size was also positive and significant ($\beta = 0.146$, $t = 2.393$, $p = 0.019$), indicating that organization size strengthens the effect of budget planning on financial performance. The study recommends investment in forecasting capability, participatory budgeting and contingency planning, and size-appropriate budgeting frameworks for SMEs. Future studies should use longitudinal designs and objective financial indicators.

KEYWORDS: *Budget Planning, Organization Size, Financial Performance, Moderating Effect, Small and Medium Enterprises, Kenya*

1.0 INTRODUCTION

1.1 Background of the Study

Budgeting is one of the oldest and most widely used management control tools. It translates organizational strategy into financial plans, coordinates the use of scarce resources and provides a benchmark against which results are later judged (Hansen & Van der Stede, 2004). Surveys of practice show that organizations continue to rely heavily on budgets for planning, even where critics argue that traditional budgeting is rigid and time-consuming (Libby & Lindsay, 2010). For SMEs, whose resources are thin and whose margin for error is small, the quality of budget planning is arguably more consequential than for large firms.

SMEs are central to the Kenyan economy. The Kenya National Bureau of Statistics (KNBS, 2016) estimated that the country had about 7.41 million micro, small and medium enterprises, which employed roughly 14.9 million people and contributed about one-third of gross domestic product. Within this sector, the top 100 SMEs represent the most successful and best-organized enterprises, so how they plan and control their finances offers an important indication of what works for growth-oriented SMEs. Despite this importance, evidence on whether formal budget planning translates into better financial performance among such firms remains limited and mixed.

One reason for the mixed evidence is that the budgeting–performance link is rarely context-free. Contingency research in management accounting has long argued that the design and effectiveness of management control systems depend on organizational characteristics, of which size is among the most prominent (Chenhall, 2003; Merchant, 1981). Larger organizations tend to have more formalized structures, specialist finance staff and better information systems, and are therefore better placed to exploit a well-prepared budget (King, Clarkson & Wallace, 2010; Lavia López & Hiebl, 2015). Smaller enterprises may prepare budgets with fewer resources and less formality, which may dilute the benefit of planning. If this is so, the effect of budget planning on financial performance should not be uniform across SMEs but should vary with organization size.

Limited work has tested this proposition for Kenyan SMEs. Jepleting, Tarus and Shitote (2024) examined budget planning and financial performance among SMEs in Eldoret Town and tested a moderator, but the moderator was digital financial services rather than organization size. Studies of the top 100 SMEs, such as Abongo (2017), have examined the budgeting process in general without testing whether organization size conditions its effect. This study therefore examined the effect of budget planning on the financial performance of the top 100 SMEs in Kenya and tested whether organization size moderates this relationship.

1.2 Statement of the Problem

1.3 Objectives of the Study

i.To establish the effect of budget planning on the financial performance of the top 100 SMEs in Kenya.
ii.To determine the moderating effect of organization size on the relationship between budget planning and the financial performance of the top 100 SMEs in Kenya.

1.4 Research Hypotheses

$H0_1$: Budget planning has no statistically significant effect on the financial performance of the top 100 SMEs in Kenya.
$H0_2$: Organization size does not significantly moderate the relationship between budget planning and the financial performance of the top 100 SMEs in Kenya.

1.5 Significance of the Study

The study will be significant to SME owners and managers, as it clarifies whether and for whom budget planning pays off, enabling better design of planning processes and allocation of scarce finance staff time. Policymakers and SME support agencies will benefit from evidence on whether budgeting support should be differentiated by enterprise size. Scholars will find the study useful as a reference point for further inquiry into how organizational scale conditions the value of management accounting practices in emerging economies.

2.0 LITERATURE REVIEW

2.1 Theoretical Framework

The study is anchored on two theoretical perspectives: Incremental Budgeting Theory and Activity-Based Costing Theory.

2.1.1 Incremental Budgeting Theory

Incremental Budgeting Theory, associated with Wildavsky (1964) and formalized in Davis, Dempster and Wildavsky (1966), holds that budgets are built from the previous period's allocations, adjusted by small increments, because decision-makers face limited information and time and wish to reduce conflict. Its attraction for SMEs is simplicity and predictability: historical allocations provide a stable starting point for planning with minimal effort. Applied to this study, the theory suggests that budget planning in many SMEs is anchored on past figures, which supports continuity but can carry forward inefficiencies and weaken forecasting accuracy when conditions change. A recognized critique is that incrementalism discourages systematic re-examination of spending and rewards inertia. The theory is useful for explaining why planning quality, particularly forecasting and contingency provision, may vary across enterprises.

2.1.2 Activity-Based Costing Theory

Activity-Based Costing (ABC) was developed in response to the distortions of traditional cost allocation (Cooper & Kaplan, 1988; Kaplan & Cooper, 1998). It assigns resource costs to activities and then to products or services according to the activities they consume, thereby improving cost visibility and directing budgets to value-creating activities. ABC-informed budget planning therefore ties resource allocation to demonstrable drivers of cost and value. The approach is demanding, however: it requires detailed data, skilled staff and supporting systems that smaller SMEs may lack. This implies that larger SMEs, with greater resources and specialist capacity, are better placed to implement sophisticated planning, which provides the theoretical basis for expecting organization size to strengthen the effect of budget planning on financial performance.

2.2 Empirical Review

Jepleting, Tarus and Shitote (2024) studied the effect of budget planning on the financial performance of 302 SMEs in Eldoret Town, Kenya, using structured questionnaires and hierarchical regression, and reported that digital financial services significantly shaped the relationship between budget planning and financial performance. The study did not consider organization size as a moderator and was confined to a single town. In Australia, King, Clarkson and Wallace (2010) surveyed small healthcare businesses and found that the adoption of written budgets was related to business size and structure, and that the use of written budgets was positively associated with performance. This supports the view that size shapes how budgeting is practised, and that budgeting is associated with better outcomes even among small firms. Evidence from other settings also points to size as a contextual factor. Joshi, Al-Mudhaki and Bremser (2003), in a survey of 54 medium and large companies in Bahrain, found that firm size influenced budgeting practices in certain respects. Lavia López and Hiebl (2015), in a comprehensive review of management accounting in SMEs, identified firm size among the contextual factors shaping the adoption and sophistication of management accounting. More broadly, Libby and Lindsay (2010) found that organizations continue to rely on traditional budgets even as they acknowledge their

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shortcomings, which underlines the importance of how well the planning stage is executed. Within the top 100 SMEs, Abongo (2017) examined the budgeting process and financial performance, but did not test organization size as a moderator.

Taken together, the literature suggests that budget planning is generally associated with better performance, that size influences how budgeting is practised, but that few studies have tested size as a moderator of the budget planning–performance relationship, and none has done so among Kenya's top 100 SMEs. This gap is addressed by the present study.

2.3 Conceptual Framework

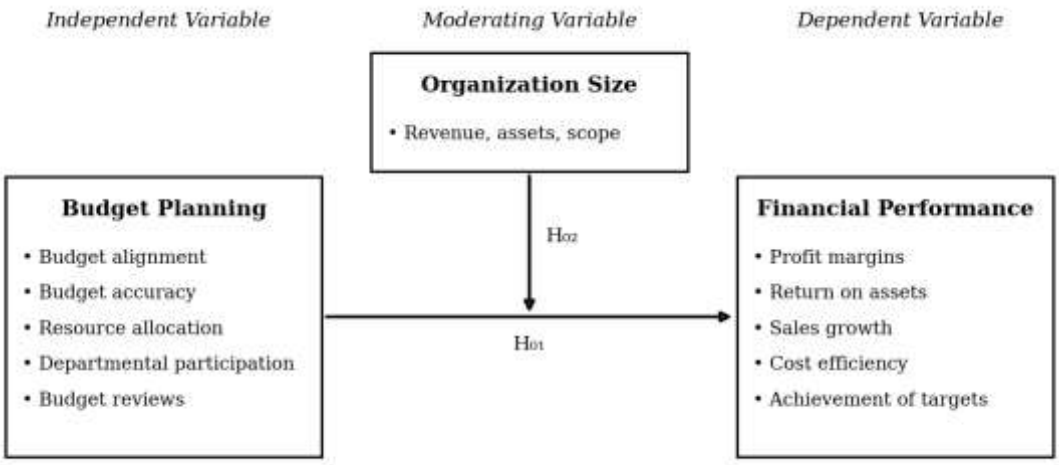


Figure 1: Conceptual Framework. Source: Researcher (2026)

3.0 RESEARCH METHODOLOGY

The study adopted a descriptive research design, which describes the characteristics of a phenomenon as it exists without manipulating variables, and is suited to testing hypothesized relationships using quantitative data (Creswell & Creswell, 2023). The target population comprised 100 Chief Accounting Officers, one from each of the top 100 SMEs on the Ministry of Trade 2021/2022 list. Chief Accounting Officers were selected because they are directly involved in budget preparation, implementation and financial decision-making. Given the small and fully identifiable population, a census was adopted, which removes sampling error because every unit is included.

Data were collected using a structured questionnaire with closed-ended items on a five-point Likert scale (1 = Strongly Disagree, 5 = Strongly Agree). Budget planning, organization size and financial performance were each measured using eight items. Budget planning items covered strategic alignment, accuracy of projections, resource allocation, budget reviews, departmental participation, management guidelines and contingency plans. Organization size items covered revenue size, asset value, market share and operational scope. Financial performance items covered profit margins, return on assets, sales growth, cost efficiency and achievement of financial targets; a composite perceptual measure was used because many SMEs are privately owned and have limited or inconsistent published financial statements. A pilot study with 10 respondents drawn from SMEs that had appeared on earlier editions of the list but not on the 2021/2022 list was used to refine the instrument. Validity was assessed through expert judgement, and reliability through Cronbach's alpha (DeVellis, 2017); all constructs exceeded the 0.70 threshold, with alpha values of 0.810 for budget planning, 0.731 for organization size and 0.713 for financial performance. Authorization was obtained from the Kabarak University Research Ethics Committee (KUREC) and the National Commission for Science, Technology and Innovation (NACOSTI) before data collection.

Data were analysed in SPSS using descriptive statistics, Pearson correlation and regression analysis. Diagnostic tests were conducted for normality (Shapiro-Wilk), multicollinearity (tolerance and variance inflation factor), heteroscedasticity (Breusch-Pagan), autocorrelation (Durbin-Watson) and linearity (Ramsey's RESET). The moderating effect was tested by introducing an interaction term between the predictor and the moderator (Baron & Kenny, 1986; Aiken & West, 1991). The direct effect model was specified as:

$$\textbf{Model 1: } Y = \beta_0 + \beta_1 X_1 + \varepsilon$$

and the moderated model as:

$$\textbf{Model 2: } Y = \beta_0 + \beta_2 (X_1 \times M) + \varepsilon$$

where Y = financial performance of the top 100 SMEs; β_0 = constant; β_1 = coefficient of budget planning; β_2 = coefficient of the interaction term; X_1 = budget planning; M = organization size (moderator); $X_1 \times M$ = interaction between budget planning and organization size; and ε = error term.

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4.0 RESULTS AND DISCUSSION

4.1 Response Rate

Questionnaires were administered to all 100 Chief Accounting Officers, of whom 83 returned completed questionnaires, a response rate of 83.0%. This exceeds the 70% level commonly regarded as excellent for survey research (Mugenda & Mugenda, 2003) and is adequate for inferential analysis.

4.2 Demographic Characteristics

Of the 83 respondents, 52 (62.7%) were male and 31 (37.3%) were female. Most respondents (42.2%) were aged 30–39 years, and 80.7% held a bachelor's or master's degree. In terms of experience, 69.8% had between 5 and 15 years, and a further 20.5% had 16 years or more. On firm maturity, 75.9% of the SMEs had operated for more than 10 years. The respondents were therefore educated, experienced and drawn from well-established firms, which supports the credibility of their perceptions of budgeting practice.

4.3 Budget Planning

Table 1: Descriptive Results for Budget Planning (%)

Statement	SD	D	N	A	SA	Mean	Std. Dev.
The organization's budget is closely aligned with strategic goals	4.8	9.6	18.1	48.2	19.3	3.68	1.045
Budget planning includes accurate and realistic projections	24.1	34.9	27.7	10.8	2.5	1.93	1.015
Resources are allocated effectively according to budget plans	15.7	25.3	30.1	22.9	6.0	2.78	1.123
Regular budget reviews support timely adjustments	4.8	8.4	15.7	50.6	20.5	3.73	1.008
All departments participate in creating the budget	27.7	36.1	25.3	9.6	1.3	1.80	0.995
Management provides clear guidelines for budget preparation	12.0	21.7	28.9	27.7	9.7	3.01	1.187
Contingency plans are included within the budget	25.3	33.7	27.7	10.8	2.5	1.94	1.020
Budget planning aligns with overall organizational objectives	5.2	10.2	19.5	47.0	18.1	3.62	1.040
Overall average						**2.81**	**1.054**

SD = Strongly Disagree, D = Disagree, N = Neutral, A = Agree, SA = Strongly Agree. N = 83.

Table 1 shows that budget planning was moderately practised (overall mean = 2.81, SD = 1.054). The strongest items concerned alignment and review: 71.1% agreed that regular budget reviews support timely adjustments (mean = 3.73), 67.5% that the budget is closely aligned with strategic goals (mean = 3.68), and 65.1% that planning aligns with organizational objectives (mean = 3.62). This indicates that the top 100 SMEs link their budgets to strategy and revisit them, which is consistent with the view that budgets serve as a coordination device between strategy and operations (Hansen & Van der Stede, 2004).

In contrast, the weakest items concerned the technical and participatory quality of planning. Only 13.3% agreed that projections are accurate and realistic (mean = 1.93), 10.9% that all departments participate in budget creation (mean = 1.80), and 13.3% that contingency plans are included (mean = 1.94). Resource allocation according to plan (mean = 2.78) and clarity of management guidelines (mean = 3.01) were rated moderately. These results suggest that many SMEs prepare budgets that are strategically aligned but weakly grounded in realistic forecasts and narrowly owned within the organization. This pattern is consistent with Incremental Budgeting Theory, under which budgets rely heavily on past allocations and are less often rebuilt around fresh projections or scenarios (Wildavsky, 1964; Davis, Dempster & Wildavsky, 1966).

4.4 Organization Size

Table 2: Descriptive Results for Organization Size (%)

Statement	SD	D	N	A	SA	Mean	Std. Dev.
Revenue size influences the effectiveness of budget management practices	5.5	11.2	13.8	47.0	22.5	3.74	1.021
Asset value supports efficient budget allocation	7.0	12.5	15.0	44.0	21.5	3.61	1.050
Market share impacts the approach to budget planning	20.0	29.5	28.0	15.0	7.5	2.61	1.120
Operational scope affects budget control and monitoring practices	7.5	13.0	17.0	45.0	17.5	3.55	1.060
Organization size determines the allocation of resources in budget processes	8.0	12.0	15.5	44.5	20.0	3.58	1.070

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Increased size presents challenges in budget adherence management	9.0	13.5	18.0	42.0	17.5	3.47	1.050
Organization size influences financial performance outcomes of budgeting	6.0	10.5	16.0	48.0	19.5	3.70	1.030
Larger organizations have greater capacity to leverage budgets for performance	7.0	11.5	17.0	46.0	18.5	3.60	1.040
Overall average						**3.48**	**1.060**

N = 83.

Table 2 shows that respondents moderately-to-strongly agreed that organization size matters for budgeting (overall mean = 3.48, SD = 1.060). The highest-rated statements were that revenue size influences the effectiveness of budget management (mean = 3.74; 69.5% agreed), that size influences financial performance outcomes of budgeting (mean = 3.70) and that asset value supports efficient budget allocation (mean = 3.61). Respondents also agreed that larger organizations have greater capacity to leverage budgets (mean = 3.60). Market share was rated lowest (mean = 2.61), suggesting that respondents associate size with internal resource base, namely revenue, assets and operational scope, rather than with market position. These perceptions are consistent with the contingency view that larger organizations possess more resources and more formalized systems with which to apply management accounting tools (Chenhall, 2003; Lavia López & Hiebl, 2015).

4.5 Financial Performance

Table 3: Descriptive Results for Financial Performance (%)

Statement	SD	D	N	A	SA	Mean	Std. Dev.
Our organization maintains strong profit margins due to effective budgeting	27.7	36.1	25.3	9.6	1.3	1.80	0.995
Budgeting processes support a higher return on assets	15.7	25.3	30.1	22.9	6.0	2.78	1.123
Sales growth is aligned with budgetary objectives and projections	26.5	34.9	24.1	11.0	3.5	1.90	1.030
Cost efficiency improves due to well-managed budget practices	3.6	6.0	12.0	57.8	20.5	3.86	0.938
Financial targets are regularly achieved due to budget adherence	18.1	27.7	30.1	18.1	6.0	2.66	1.173
Profitability is closely linked to adherence to budget plans	16.9	24.1	28.9	24.1	6.0	2.79	1.135
Financial goals are more achievable through rigorous budget controls	4.8	7.2	14.5	55.4	18.1	3.75	0.980
Financial performance improves with disciplined budget management	5.2	8.5	16.0	52.0	18.3	3.70	1.010
Overall average						**2.90**	**1.048**

N = 83.

Financial performance was moderate overall (mean = 2.90, SD = 1.048). Respondents most strongly agreed that cost efficiency improves with well-managed budgets (mean = 3.86; 78.3% agreed), that financial goals are more achievable through rigorous budget controls (mean = 3.75) and that financial performance improves with disciplined budget management (mean = 3.70). Outcomes that depend on the market, however, were rated far lower: strong profit margins (mean = 1.80), sales growth in line with budgeted projections (mean = 1.90) and regular achievement of financial targets (mean = 2.66). The pattern implies that budgeting is credited mainly with improving cost discipline, while profitability and growth, which also depend on demand and competition, remain weaker. The low rating for sales growth aligned with budget projections is consistent with the weak forecasting accuracy observed in Table 1.

4.6 Diagnostic Tests

The regression assumptions were satisfied. Residuals were normally distributed (Shapiro-Wilk p = 0.387). Multicollinearity was not severe, with tolerance values between 0.180 and 0.200 and variance inflation factors between 5.000 and 5.556, below the threshold of 10 recommended by Hair, Black, Babin and Anderson (2019); the VIF for budget planning was 5.208. The Breusch-Pagan test indicated homoscedasticity ($\chi^2 = 2.124$, p = 0.547), the Durbin-Watson statistic of 1.897 indicated no autocorrelation (Field, 2018), and Ramsey's RESET test showed no significant departure from linearity (F = 1.098, p = 0.356).

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4.7 Correlation Analysis

Table 4: Correlation Analysis (N = 83)

Variable	Budget Planning	Organization Size	Financial Performance
Budget Planning	1.000	0.483**	0.678**
Organization Size	0.483**	1.000	0.667**
Financial Performance	0.678**	0.667**	1.000

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

Budget planning was positively and significantly correlated with financial performance ($r = 0.678$, $p < 0.01$), indicating that SMEs with stronger planning practices tended to report better financial performance. Organization size was also strongly correlated with financial performance ($r = 0.667$, $p < 0.01$) and moderately correlated with budget planning ($r = 0.483$, $p < 0.01$). The moderate correlation between budget planning and organization size shows that the two constructs are related but sufficiently distinct to justify testing size as a moderator rather than treating it as a duplicate measure of planning quality.

4.8 Regression Analysis

Table 5: Regression Coefficients

Model	Variable	B	Std. Error	Beta	t	Sig.
1	(Constant)	0.157	0.084	—	1.869	.065
	Budget Planning	0.325	0.086	0.325	3.779	.000
2	(Constant)	0.140	0.082	—	1.707	.092
	Budget Planning × Organization Size	0.146	0.061	0.146	2.393	.019

Dependent variable: Financial performance.

Budget planning had a positive and statistically significant effect on financial performance ($B = 0.325$, $\beta = 0.325$, $t = 3.779$, $p < 0.001$). Holding the other budget process dimensions constant, a one-unit improvement in budget planning is associated with a 0.325-unit increase in financial performance. The effect is consistent with Jepleting, Tarus and Shitote (2024), who also found budget planning to be associated with SME financial performance in Kenya, and with King, Clarkson and Wallace (2010), who found written budgets to be positively associated with performance in small businesses. The result also resonates with the descriptive findings: although forecasting accuracy, participation and contingency planning were weak (Table 1), the planning practices that were strong, namely strategic alignment and regular review, appear sufficient to produce a measurable performance benefit, implying that improving the weak areas could yield further gains.

The interaction between budget planning and organization size was positive and significant ($B = 0.146$, $\beta = 0.146$, $t = 2.393$, $p = 0.019$). This shows that the relationship between budget planning and financial performance is stronger in larger SMEs. Substantively, larger enterprises appear to convert planning effort into better results more effectively, which is consistent with the resource and capability argument of Activity-Based Costing Theory, under which larger firms have the data, expertise and systems to apply more sophisticated planning (Kaplan & Cooper, 1998), and with contingency evidence that size shapes budgeting practice (King et al., 2010; Joshi et al., 2003; Lavia López & Hiebl, 2015). Including the interaction terms raised explained variance in the full model from 61.3 to 68.5%. The estimated equations, with the other budget process terms in the full models omitted for brevity, are:

$$\textbf{Model 1: } Y = 0.157 + 0.325X_1$$
$$\textbf{Model 2: } Y = 0.140 + 0.146(X_1 \times M)$$

4.9 Hypothesis Testing

Table 6: Hypothesis Testing Results

Hypothesis	Variable	β	p-value	Decision
$H0_1$	Budget Planning	0.325	0.000	Rejected
$H0_2$	Budget Planning × Organization Size	0.146	0.019	Rejected

Since both p-values were below 0.05, both null hypotheses were rejected. Budget planning significantly affects the financial performance of the top 100 SMEs in Kenya, and organization size significantly moderates this relationship.

5.0 CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions

The study concludes that budget planning has a positive and statistically significant effect on the financial performance of the top 100 SMEs in Kenya. Planning in these firms is moderately practised: it is strong on strategic alignment and regular review, but weak on forecasting accuracy, departmental participation and contingency planning. These weaknesses are consistent with an incremental approach in which budgets lean on past allocations, and they appear to limit the extent to which planning translates into profitability and sales growth, even as it improves cost efficiency. The study further concludes that organization size significantly moderates the relationship, such that budget planning yields a stronger performance benefit in larger SMEs, where greater resources, capacity and formal systems allow planning to be executed and exploited more effectively.

5.2 Recommendations

SME managers should strengthen the technical quality of budget planning by investing in forecasting capability, building scenario and contingency provisions into budgets, and involving departments in budget preparation, while retaining the strategic alignment and regular reviews that are already working. SME support agencies and professional bodies should provide training and practical planning tools in these areas. Because the benefit of planning is larger in bigger firms, support programmes should be differentiated by size: simplified, low-cost planning templates and capacity building for smaller SMEs, and more advanced cost-driver-based planning for larger ones. Smaller SMEs in particular should be supported to close the capability gap that appears to limit their returns from planning.

The study relied on perceptual self-reported measures from a single respondent per firm and on cross-sectional data, which limits causal inference and may introduce common-method bias. Future studies should use longitudinal designs, combine perceptual measures with audited financial indicators such as return on assets, measure organization size objectively (for example by employees or turnover), and test additional moderators such as technology adoption and market volatility.

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